البنك الوطني العماني
NBO

ANNUAL REPORT 2017

البنك الوطني العماني
NBO

National Bank of Oman
P.O. Box 751
Ruwi, Muscat
Sultanate of Oman

nbo.om

HIS MAJESTY SULTAN QABOOS BIN SAID

Content

Chairperson's Report - 2017

Dear Shareholder,

On behalf of the Board of Directors of National Bank of Oman SAOG, I am pleased to present the financial results and the accompanying financial statements for the year ended 31st December 2017.

An eventful year

In 2017, the GCC region recorded 0.5 per cent GDP growth – its weakest in eight years. The macroeconomic environment was affected by high levels of volatility in the financial markets, with continued declines in commodity prices and uncertainty related to some of the advanced economies.

In addition we saw increased asset quality stress in the UAE as the Oil price crash resulted in key sectorial weaknesses.

Against this backdrop, we made good progress on our strategy and delivered solid returns, but these headwinds resulted in a lower overall net profit for 2017. These results are commendable given economic challenges which reduced customer activity, as well as the collapse of oil prices which caused stress across key sectors and our foreign operations.

A strong, resilient franchise

We delivered net attributable profit of OMR 44m, a reduction of 21 per cent compared to the previous year – primarily due to margin compression on account of higher funding costs and higher loan loss provisions in UAE.

While we continue to maintain the highest spread amongst peer banks, net interest income from conventional banking and revenues from Islamic financing activities decreased by 8.5 per cent to OMR 92.9 million, primarily due to higher deposit costs.

The Bank continues to focus on garnering low cost deposits and diversify its deposit base in an effort to minimize deposit costs as well as reduce concentration.

Non-interest income grew strongly by 13.5 per cent to OMR 39.2 million. It is pleasing to note that the Bank's strategic agenda to diversify fee income has started yielding positive results and the bank will continue to focus its efforts to increase fee income given the tough market conditions in growing loans.

Given the pressure on income, operating costs have been tightly managed and have increased by a modest 3 per cent over last year. The bank's cost to income ratio stood at 48.8 per cent as compared to 46 per cent in the last year.

Impairments on loans and advances have increased to OMR 16.4 million compared to OMR 10 million during the same period last year. This adverse variance arises due to elevated provisions in our UAE book. The loan loss coverage as at 31 December was at 104 per cent, but the bank is holding collaterals on certain impaired loans.

2017 continued to be a challenging year for the bank's UAE business in terms of maintaining quality assets, which was as per expectations during this stage of the economic cycle. To adopt to the changing market conditions active measures were taken to acclimatize credit and operational controls in the UAE. The bank has taken prudent provisions levels to guard against the adverse changes in the credit quality within the market.

We introduced diversification plans to reposition the UAE operations to capture trade opportunities targeting Omani businesses operating across the Oman and UAE borders.

The bank's capital adequacy ratio after the proposed dividend pay-out is 17.34 per cent and after taking the estimated one-off IFRS 9 reserve adjustment is projected at 15.97 per cent, against the regulatory requirement of 13.875 per cent. The bank's core equity ratio stands at 12.6 per cent, against the regulatory requirement of 8.875 per cent reflecting the bank's very robust capital position.

Given the challenging operating environment, the Board and senior management are very pleased with how we were able to manage our risks, maintain equity returns above the market and grow the business sensibly.

The bank of choice

In 2017, we continued to make progress in our transformation process. We began this process some years ago and are ahead of the rest of the industry, with a multi-dimensional vision that includes a three-pronged approach:

Compelling Solutions

By thinking deeply about customers' true needs, we can make their banking truly simple and relevant.

Our aim is to provide the best solutions through simple, transparent and easy-to-contract products. We focus on innovative solutions that really matter to our customers and improve the quality of their daily lives.

Retail banking focussed on developing the best in class wealth management solutions for high net worth clients while expanding its non-lending solutions in the areas of insurance, remittances and card services.

Wholesale banking continued to demonstrate its commitment to our corporate and government clients in the most practical way possible – by helping them to grow – with industry leading working capital and cash management solutions supported by a world class digital platform.

Investment banking continued to play a key advisory role for our clients to help them navigate these economic conditions and provided strategic advisory on key merger and acquisition deals.

In addition, we strengthened our linkage between our Oman and UAE operations with a first-of-its-kind seamless banking solution, allowing our Omani clients to effortlessly trade and manage their operations across borders.

Muzn Islamic Banking also enhanced its product and service offerings by launching the new private banking offering, and was also voted the best Islamic banking service provider in Oman.

Finally, we know that some of the best ideas come from outside the bank, from our customers themselves and the communities in which we operate. To this end, NBO proudly hosted the Sultanate's first ever Hackathon, with over 300 students, start-ups, and entrepreneurs from various corners of the country and the region participating, all with a single goal to re-imagine banking.

The competition has set a precedent across the country's banking sector, with the aim of inspiring a new way of thinking that focuses on value creation, as well as new sources of revenue through innovation and technology.

Superior Customer Experience

To become more customer-centric, we have made it a priority to embed ourselves in the customer's journey. This means thinking about banking not as a separate activity, but as one that should be seamlessly interwoven into a customer's everyday life.

Thanks to our investment in technology, the number of customers using our digital banking services rose by more than 90 per cent in 2017. Our mobile and online banking solutions now account for over 60 per cent of all customer service transactions, allowing us to focus the branches on more complex value added services to our customers. The adoption of digital banking by our customers has exceeded all of our expectations.

We also continue to look for ways in which we can serve our customers in the traditional sense during their day to day interactions. One example is our cashless payment solution at all McDonalds' outlets across the country.

We also continue to invest in key digital experiments, investments that will make a significant difference in our customers' lives in the future. In March, for example, the bank became the first in Oman to announce the successful completion of the international remittances pilot project using block chain technology - a technology that can help our customers transfer money internationally in seconds rather than days.

First Class Workforce

Finally, we are re-wiring the organisation to create a high performance culture, a culture that embraces innovation and new ways of working.

We believe that we must have a work environment that is empowering. At the same time, we need to be relentless about up skilling our people.

We therefore invest heavily in them every year, and the importance of their continuous development played a major role in our decision to build our new headquarters, which we proudly inaugurated in November.

Our new headquarters is meant to act as incubation hub for our talent and improve our ability to collaborate and partner on new ideas that solve our customers' problems.

NBO was the first bank to incorporate innovation into our talent development. To inculcate a digital mind set and spur innovation, the bank established a platform called Ibtikar in 2014 that has run over 60 experiments to date. During these experiments, employees work to create prototype mobile apps to address business problems and we often test these innovations at the new head office branch with our customers before it is rolled out nationally.

This enables them to gain exposure to the fintech culture, agile methodology and other digital working concepts - giving our people the exposure they need so we can innovate as a bank.

Sustainability

Sustainability has always been at the core of our purpose-driven DNA. We recognise that not all returns can be found in financial statements and that our responsibility to shareholders is complemented by responsibility to society at large.

NBO has worked hard to build relationships and work together with other both public and private entities to support the Sultanate's long-term economic diversification agenda.

The bank lends its full support to the sector through numerous initiatives, events and sponsorships, including the NBO Golf Classic event, which has promoted the Sultanate to a global audience and put Oman on the world golf map.

During 2017, we also continued to support entrepreneurs and SMEs, encourage innovation, fund key projects of national importance, inspire women to achieve personal and professional fulfilment, and inspire the country's young population.

In recognition of this commitment, NBO was recently named the 'Best Financial Support' at the third edition of the Entrepreneurship Awards held under the patronage of H.E. Sheikh Abdulmalik bin Abdullah Al Khalili, Minister of Justice.

The award recognized NBO as a financial institution that effectively supports and funds small and medium enterprises.

Dividends

The board has recommended dividends at levels similar to last year. The Bank remains well capitalized in preparation for all regulatory changes including IFRS 9.

Looking Forward

We expect 2018 to continue to be challenging. Our base case is that the regional economy will be somewhat better, backed by stronger oil prices and improvements to the non-oil sector. The rise in oil prices, if remains permanent could ease the quantum of borrowing necessary to bridge the deficit.

The banking operating environment is expected to be subdued during most part of 2018 characterized by tighter liquidity, rising deposit rates and asset quality pressures.

Our core business will remain stable, helped by the potential pickup in interest rates, active risk management especially in the UAE, unlocking cost efficiency through our investments in digital, as well as execution of our strategy to build new diversified fee generating solutions across all of our business lines.

Furthermore, the Bank continuously looks at ways of achieving better synergies with its strategic partners and affiliates in business transactions as well as sharing best practices.

We remain committed to improving our ROE up through our target range.

In line with our values we will execute our strategy by placing our clients at the centre of everything we do; working to earn and keep our clients' and stakeholders' trust.

I would like to congratulate the more than 1,500 men and women who work at NBO around the region and who make us a better bank. I encourage them to continue working with the same enthusiasm and dedication.

On behalf of the whole NBO team, we thank our customers, shareholders, regulators, partners and the wider community for their continuous support throughout the year. We are proud to serve them and look forward to delivering further success in 2018.

Above all, we pay tribute to His Majesty, Sultan Qaboos Bin Said, for his inspiring leadership and vision and under whose wise guidance Oman steadfastly continues on its path towards successful development.

It is a great privilege to be part of this great institution and to help drive Oman's growth and development. NBO is firmly on track towards executing our strategy, achieving our vision and fulfilling our purpose.

Rawan bint Ahmed Al Said

Chairperson

Chairperson's Report - 2017

Mr Ghassan Khamis Al Hashar
Director

Ms. Amal Suhail Bahwan
Director

H.E. Mr. Abdul Rahman
Bin Hamad Al Attiyah
Director

Mrs. Najat Ali Al Lawatia
Director

Mr. Rahul Kar
Director

Mr. Mohammed Ismail
Mandani Al Emadi
Director

Mr. Hamad Mohammad
Hamood Al Wahaibi
Director

Mr. Rashid Bin Saif Al-Saadi
Director

Mr. Fahad Badar
Director

Sayyidah Rawan Al Said
Chairperson

H.E. Sheikh Abdulla bin Ali bin
Jabor Al Thani
Deputy Chairman

Board of Directors

Board Members Profiles

Chairperson of the ENRC. Dr. Sayyida Rawan Ahmed Al Said is the CEO of Takaful Oman SAOG, Prior to joining Takaful Oman, she was the Managing Director and CEO of ONIC Holding Corporation. Before moving to the Private Sector, Rawan was the Deputy CEO-Investment for the State General Reserve Fund of Oman, leading the execution of many mega investments internationally. She has almost 30 years of experience in the financial industry, 20 of which are in the Public sector.

She has been a member on the Board of a number of reputed Companies and Financial Institutions in Public and private sector in Oman and in the region. Chairperson in National Bank of Oman, Deputy Chairperson in Oman Oil Marketing Company, Board Member of Oman National Investments Development Company ONIDCO (Tanmia). Public companies she was the Board Member of Oman Oil Company SOAC and its Audit Committee. Chairperson of its Equity and GCC Funds. Board Member in International General Insurance (IGI) Jordan, and National Finance House (NFH), Bahrain. Deputy Chairman of Orix Finance, National Life & General Insurance Company SAOC (NLIG) and Al Ahlia Insurance.

She is also a Member on the Investment Committee of the Public Authority for Social Insurance, Board Member in Public Authority for the SME Development (Riyada). Chairperson of Al Kawther Fund (Islamic Compliant Fund) and a Member of the Investment Committee of Orphans & Incapacitated Funds in the Ministry of Justice. She has been recently appointed as a Board member of the Sultan Qaboos University Council.

Sayyida Rawan remains to be the First and the only Female who holds a CEO position in a public listed company in Oman.

In 2011, She was bestowed the Business Professional (BizPro) Leader Award. In 2012, was ranked 14th in Forbes Middle East for the 'Most Powerful Arab Business Women in Listed Companies'. In 2014, Rawan was named among the Best Chief Executives in the region by Trend in collaboration with INSEAD (The Business School for the World). Also she was Awarded Hall of Fame by MARA Excellence Awards. In 2015, she was honored with two prestigious Awards; Asian Women Leadership of the Year from World Leadership Congress and in MENA and Business Leader of the year from the Middle East Accountancy and Finance Excellency Awards 2015. In 2016 she was honored with Honorary Doctorate Degree from Commonwealth University in UK and she was awarded as the Best Takaful CEO from Global Business Outlook, UK. In 2017 she won the best Takaful CEO-Oman, International Finance, London. Dr. Rawan ranked 3rd in Oman for Forbes the Top 100 most powerful Arab Businesswomen 2017.

Dr. Sayyida Rawan, has an MSc in Economics &Finance from Loughborough University UK. She also holds a Post Graduate Diploma in Investment Analysis from Stirling University UK, and BA in Economics & Political Science from the American University in Cairo (AUC).

Sayyida Rawan Ahmed Al Said,
Chairperson

Member of the Executive, Nomination and Remuneration Committee (ENRC).

H.E. Sheikh Abdulla bin Ali bin Jabor Al Thani has been a Director of the Bank since July 2005 and serves as a member of the Board Executive, Nomination and Remuneration Committee (ENRC). His Excellency is the Chairman of The Commercial Bank (P.S.Q.C.) in Qatar, a member of the Board of Directors for United Arab Bank, P.J.S.C. in UAE and is the Owner of Vista Trading Company (Qatar), a Partner in Dar Al Manar (Qatar), Domopan Qatar and Integrated Intelligence Services Company (Qatar).

H.E. Sheikh Abdulla bin Ali bin Jabor Al Thani holds a Bachelor of Arts Degree in Social Science from Qatar University.

H.E. Sheikh Abdulla bin Ali bin Jabor Al Thani,
Deputy Chairman

Member of the Board Risk Committee (BRC).

His Excellency Abdul Rahman Bin Hamad Al Attiyah has been a Director of the Bank since November 2014. He serves as a member of the Board Risk Committee (BRC) and is a member of the Board of The Commercial Bank (P.S.Q.C.) since March 2014. He began his career in 1972 at Qatar's Ministry of Foreign Affairs and has served as Qatar's Ambassador in Geneva, Saudi Arabia, France, Italy, Greece, Switzerland, Yemen, and Djibouti. He also served as a permanent representative to the United Nations in Geneva, the Food and Agriculture Organization (FAO) in Rome, and UNESCO in Paris. He is the Minister of State of Qatar and holder of the state award of appreciation.

His Excellency Al Attiyah was the former Secretary-General of the Gulf Cooperation Council (GCC) from 2002 until 2011. He holds a Bachelor of Arts Degree in Political Science and Geography from the University of Miami, United States of America. He is the owner and Chairman of Mawten Trading in Qatar and Vice President of the Board of Trustees of the Arab Thought Forum – Amman, Jordan.

His Excellency Mr. Abdul Rahman Bin Hamad Al Attiyah,
Director

Member of the Executive, Nomination and Remuneration Committee (ENRC) and the Board Risk Committee (BRC).

Ms. Amal Suhail Bahwan is the Vice Chairperson of Suhail Bahwan Group Holding LLC. She has extensive experience in managing companies across the Bahwan Group.

She is also the Chairperson of Oman Ceramics SAOG, Director and Executive Committee member of National Pharmaceutical Industries SAOG and Director of Oman Oil Marketing Co SAOG.

Ms. Amal has a Bachelor's degree in Education and a Master's degree in Administration from the Sultan Qaboos University.

Ms. Amal Suhail Bahwan,
Director

Board of Directors

Board Members Profiles

Member of the Board Audit Committee (BAC) and the Board Risk Committee (BRC).

Mr Al Hashar joined NBO Board as a representative of the Public Authority for Social Insurance (PASI) in March 2017. He is currently the Authority's Director of Investments. He has nearly 20 years of experience in finance and investment management, and represents PASI on the boards of numerous public and private companies. He is also the Chairman of Muscat Fund Management Body and Board Director at Oman National Investments Development Company SAOC (TANMIA).

Mr. Al Hashar holds a Master's Degree in Finance and Investment Management.

Mr Ghassan Khamis Al Hashar,
Director

Chairperson of the Board Risk Committee (BRC) and Member of the Board Audit Committee (BAC).

Mr. Mohammed Ismail Mandani Al Emadi has been a Director of the Bank since November 2014. He is also a member of the Board for The Commercial Bank (P.S.Q.C.) and a member of the Board of Alternatifbank A.S. (ABank), Turkey and has over 30 years of banking experience. Mr. Al Emadi has held a number of key roles at Commercial Bank until 2006, after which he served as Chief Executive Officer of Qatar Real Estate Investment Company Q.S.C. up to 2011, and also served as its Director from 2003 until 2005.

Mr. Al Emadi holds a Bachelor of Arts Degree in Business Administration and Economics from Holy Names University, California.

Mr. Mohammed Ismail Mandani Al Emadi,
Director

Chairperson of the Board Audit Committee (BAC).

Mr. Rahul Kar has been a Director of the Bank since April 2016. Mr. Kar is a Chartered Accountant with over 25 years of relevant experience and is currently working as the Financial Advisor to the Chairman of Suhail Bahwan Group Holding LLC.

Mr. Rahul is also a Director and an Audit committee member of National Pharmaceutical Industries SAOG and Al Suwadi Power Co SAOG. He is also a Director and Nomination & Remuneration committee member of Oman United Insurance Company SAOG.

Mr. Rahul Kar,
Director

Member of Credit Committee of the Board (CCB).

Ms. Najat Ali Al Lawatia was elected as a Director of the Bank at the AGM in March 2017. She holds a Commerce Degree in accounting and has attended various courses in diverse fields of financial management, audit, investments etc. She is working as the Deputy Director General-Support Services with Civil Service Employees Pension Fund and has more than 20 years of relevant experience.

Ms. Najat is also a Director and Chairperson of Audit Committee of Oman Cement Company SAOG.

Mrs. Najat Ali Al Lawatia,
Director

Member of the Credit Committee of the Board (CCB).

Mr. Fahad Badar has been a Director of the Bank since May 2016. He is also a member of the Board for Alternatifbank A.S. (ABank), Turkey since September 2013 and a member of the Board for ALease, Turkey since March 2016. He is also a member of the Board for United Arab Bank, P.J.S.C. in UAE since July 2016.

Mr. Badar's career at The Commercial Bank (P.S.Q.C.) in Qatar spans over 17 years. Prior to his current role as Executive General Manager, International Banking, he held a number of key roles in International Banking, the Government and Public Sector Relations and the Wholesale Banking Divisions.

Mr. Badar holds an MBA from Durham University, UK and a Bachelor of Arts Degree in Banking & Finance from the University of Wales.

Mr. Fahad Badar,
Director

Member of the Board Audit Committee (BAC) and a member of the Credit Committee of the Board (CCB).

Member of the Board of Directors since August 2017. Mr. Rashid is a renowned financial & investment banker, business executive, entrepreneur and philanthropist best known as the CEO of TANMIA, a company that contributes to the Sultanate's economic development by joining with the right partners for the necessitated projects. An experienced Finance & investment professional, he holds a B.Sc. in Business Administration from Rollins College, USA, and has spent his career working with investors, professionals, foreign nationals, high net worth individuals and Government offices.

Mr. Rashid began his career with Diwan of Royal Court, where he worked for 12 years in various senior positions. He was involved in various committees such as Omanization, Personal Regulations & Budget to name a few. Thereafter, he joined as General Manager with Arab Management Service.

Mr. Rashid has been associated with TANMIA since 2000 and has served as its Chief Executive Officer. There were many new ventures such as GCC Investment Fund, PE Fund, and the Sharia Fund along with major direct investment initiatives such as Almouj Muscat , Takaful Oman, and Oman Hospitality company (Kempenski Oman , Octal, and so on).

Mr. Rashid regularly attends conferences worldwide on the topics of Management, finance and Investments, Emerging Markets, Private Equity, Venture Capital and Entrepreneurship.

Currently he is the Chairman of Board of Directors of Takaful Oman SAOG & A'saffa Foods SAOG. He also sits as Director on the Board of Oman Orix leasing Company, Minerals Development Company SAOC and Muscat National Development and Investment SAOC.

Mr. Rashid Bin Saif Al-Saadi,
Director

Chairperson of the Credit Committee of the Board (CCB) and member of the Board Executive, Nomination and Remuneration Committee (ENRC).

Mr. Hamad Mohammed Al Wahaibi has been a Director of the Bank since March 2014. He has 18 years of experience in the GCC. He has been a director of investment with the Ministry of Defense Pension Fund for the past five years. Mr. Al Wahaibi is also a member of the boards of Voltamp Energy Company, Al Madina Takaful Company and ACWA Power Company.

Mr. Al Wahaibi holds a Masters of Business Administration (MBA) degree, specializing in Finance, and he is a Chartered Financial Analyst (CFA) charter holder, as well as a Chartered Alternative Investment Analyst (CAIA) charter holder.

Mr. Hamad Mohammad Hamood Al Wahaibi,
Director

Executive Management

1. **Ahmed Jaffer Al Musalmi** / Chief Executive Office
2. **Faizal Eledath** / General Manager, Chief Transformation Officer
3. **Nasser Salim Al Rashdi** / General Manager, Chief Commercial Banking Officer
4. **John Chang** / General Manager, Chief Retail Banking Officer
5. **Nasser Al Hajri** / Chief Corporate Services Officer
6. **Mohammad Saif Ullah Khan** / Head, Compliance
7. **Al Sayyid Wasfi bin Jamshid Al Said** / Acting Chief Executive Officer
8. **Ananthraman Venkat** / General Manager, Chief Financial Officer
9. **Hassan Abdul Amir Shaban** / General Manager, Chief Government Banking Officer
10. **Kumar Keswani** / General Manager, Chief Corporate Banking Officer
11. **Salma Al Jaaidi** / General Manager, Chief Risk officer
12. **Hamood Khalfan Al Aisri** / Chief Internal Auditor

Our Vision, Values & Strategic Objectives

Our Vision

To be The Bank of Choice

Our Values

Customer 1st

Execution

One Bank

Integrity

Quality

Our Strategic Objectives

- Customers: The best bank in service, value and convenience for our target customer segments.
- Employees: The best workplace and career opportunities for our employees.
- Shareholders: The highest return on equity and sustainability for our shareholders.
- Community: For You. For Our Nation.

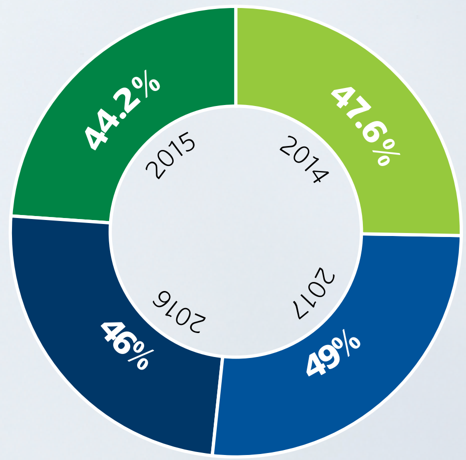
Management Discussion and Analysis Report 2017

132.1
Total Income
(in OMR million)

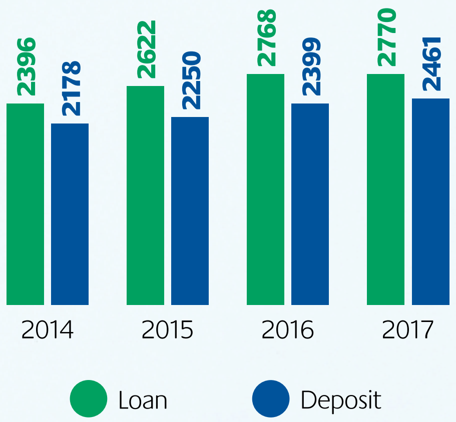
431
Shareholders' Funds
(in OMR million)

Cost to income

In our endeavor to streamline our processes, drive efficiencies and optimize costs to deliver superior value to our customers, we have taken a number of proactive measures to rationalize costs across the Bank.



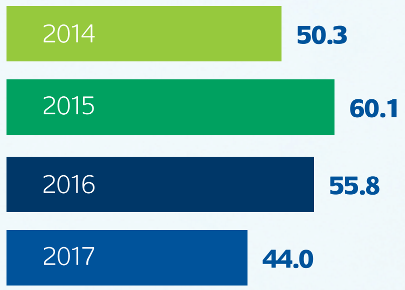
Loan and deposit
(in OMR million)



2770
The Bank continues to maintain a strong focus on high quality assets

2461
Customer deposits continue to show a steady growth

Net profit
(in OMR million)



44.0 Despite the challenging macroeconomic environment, NBO achieved good progress in diversifying its revenue streams by growing fee income. While the Bank reported a net profit of OMR 44 million in 2017, the decline is primarily due to margin compressions on account of higher funding costs and higher loan loss provisions in the UAE

1.2%
Return on Averege Assets
(in % for 2017)

Capital Adequacy
(in % for 2017)

17.3%

- Core Capital 12.6%
- AT-1 3.6%

Return on Averege Equity

10.4%	13.7%	15.9%	15.1%
2017	2016	2015	2014

Hightest return on equity and return on assets in the industry

Management Discussion and Analysis Report 2017

Ahmed Al Musalmi
Chief Executive Officer

Introduction

Driven by NBO's highly trained and experienced team of financial service professionals, the Bank extended its proven business model and prudent commercial strategy into 2017. However, 2017 was not without its challenges, through hard work, determination and an unwavering commitment to being the people's 'Bank of Choice' in Oman, we continued to lead the market by consistently demonstrating our superior service culture, latest technological innovations and diverse range of product and service offerings.

We have always recognised that the customer is at the heart of everything we do, and continued to allocate significant resources to deliver superior value, improve interaction experience and enhance delivery standards.

Behind this high-performance, customer-centric culture is a strong and valuable force, our employees. Their commitment to the organisation transcends every level of the business, which ultimately translates to customer touch points. We are determined to maintain the best and happiest workforce by creating a culture of continuous improvement and a nurturing environment for employee development. Year on year, we have invested in our employees and have given them opportunities to learn, advance, grow, improve and create.

For more than four decades, NBO has continuously invested in key pillars of the economy to help transform Oman into a sustainable knowledge-based country. The opening of our new Head Office was a testament to this, and marks a new era for the Sultanate's banking sector.

A solid business and financial partner, NBO has demonstrated its flexibility and stability in light of current market conditions. According to the recently published Fitch Rating report, the Bank has successfully implemented a long term business strategy resulting in the development of a diversified and quality portfolio of loans and deposits while remaining well capitalized with sufficient liquidity and robust profitability. This unwavering performance has enabled NBO to play a leading role in supporting Oman's socioeconomic progress and contributing to the national economic diversification agenda.

Beyond our business, our values and responsibilities have helped improve and positively impact communities across the country. During 2017, we supported entrepreneurs and SMEs, encouraged innovation, promoted the Sultanate's tourism and sports sectors, funded key projects of national importance, and inspired youth across the country, all in efforts to propel the development of the country and build a brighter tomorrow.

Operating Environment

In a period beset by global economic uncertainty, the operating environment throughout 2017 has been challenging especially with cost of funds continuing to rise, suppressed credit growth, downgrades to sovereign credit ratings and outlook of banks moving from stable to negative.

Globally and particularly in the GCC, the banking industry is experiencing a steady decline in spreads as traditional banking products are commoditized and disrupted by Fintechs.

Fiscal consolidation and prolonged low oil price have also affected Oman's economic progress. Government and large corporate spending has also slowed down as evident from credit growth.

While the economic headwinds remain, the Government continues to implement strategies to encourage diversification. These include the introduction of new taxes and reforms to cut spending and boost private sector activity over the medium and long term.

NBO in 2017

Despite the challenging macroeconomic environment, NBO achieved good progress in diversifying its revenue streams by growing fee income. While the Bank reported a net profit of OMR 44 million in 2017, the decline is primarily due to margin compressions on account of higher funding costs and higher loan loss provisions in the UAE. We took several corrective actions and strategic adjustments in response to these macro

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adverse developments in addition to successfully completing several initiatives that position NBO for future growth.

Fee Income Diversification: The Bank's strategic focus on diversifying and growing fee income streams has yielded positive results in 2017, with a growth of 6.1 percent in fee income achieved during the first nine months of 2017. This will continue to be a key strategic area for the bank.

Cost Rationalization: In our endeavor to streamline our processes, drive efficiencies and optimize costs to deliver superior value to our customers, we have taken a number of proactive measures to rationalize costs across the Bank.

Driving our Growth Strategy Forward: We advanced our growth strategy by developing new business models, strengthening our leadership team and introducing new value propositions that focus on our target segments.

Sharpening our Focus on Asset Quality: We maintained strict vigil over asset quality and de-risking our overall portfolio, this included the integration of a monitoring and early warning system for key sectors.

Maintaining Interest Margins: The Bank took several measures including re-pricing existing loans and increasing on-boarding yields for both Corporate and Retail customers. As a result, the Bank's interest margins are the best in the industry.

Enhancing Customers' Banking Experience through Innovation and Digital Leadership.

Perhaps most notably in 2017, NBO dedicated significant resources to develop and deliver innovative products and services that offer superior customer experiences, and strategically support important pillars of the economy.

In March, for example, the Bank became the first in Oman to announce the successful completion of the international remittances pilot project using block-chain technology. This further underscored NBO's position as a front-runner in digital banking solutions.

The Bank also launched a number of innovative solutions give NBO competitive edge in terms of its range and scale of its product and service offering. This included the launch of wearable banking, cards marketplace, Twitter Enquiry Service and many other banking innovations.

Supporting Oman's Strategic Economic Agenda

NBO has also worked hard to build relationships with both public and private sector entities to support the Sultanate's long-term economic diversification agenda. At the start of the year, the Bank signed a partnership agreement with the Ministry of Civil Services to share knowledge and expertise in the areas of planning, human resources, training and development.

This year NBO was also recognised by the Ministry of Sports for promoting Oman's sports sector. The Bank extended its full support through numerous initiatives, events and sponsorships, including the NBO Golf Classic, a staple event which we have fully supported for the last four years. As a result, we have showcased the Sultanate as a top sports and tourism destination, but to also given the world a view of the vast opportunities Oman has to offer.

To end a successful year, NBO unveiled its spectacular headquarters under the auspices of His Highness Sayyid Asaad bin Tariq Al Said, Deputy Prime Minister for International Relations and Cooperation Affairs and Personal Representative of His Majesty the Sultan, ushering in a new era for both the Bank and the country's financial services sector. The landmark complements Muscat's skyline, representing the country's push to achieve wider social and economic objectives. From our new home, we could not be more proud to serve the country for years to come.

Simplifying our Core Businesses

Delivering Compelling Solutions & a Superior Customer Experience

We continued our journey in 2017 in building a robust retail operation with multiple delivery channels. The focus areas centered on creating a seamless banking experience and operational effectiveness by introducing cutting-edge products and services that enhanced our customer offering. Our values of customer first, one Bank, execution, quality and integrity were and continue to be the driving engine of retail banking.

The Al Kanz scheme was designed to promote a saving culture by enabling customers to win cash prizes without risking capital. After running for 20 years successfully, the scheme was updated in 2017 to ensure that customers from each region of the Sultanate were guaranteed a chance to win. This included rewards dedicated solely to NBO's Youth Banking customers. By the end of 2017, a total of OMR 3.251 million was awarded as prize money.

Our most premium proposition, Sadara Wealth Management, saw a 300% growth in Fee Income, further reinforcing the proposition's appeal in terms of the expertise offered by the wealth management team and the tailor-made solutions available to maximize customers' wealth.

We have moved steadfast in our mission to transform Oman to a cashless society, through introducing new capabilities in the digital and mobile spheres. As the banking era continues to evolve, at the heart of all of our retail services is our digital banking platform led by the NBO app. Moving forward, we are planning to utilise the app to provide customers with value-

added services that will make customers' lives easier. This includes ensuring complete digitalization, establishing a solid data infrastructure and integrating the usage of AI technology.

The Bank was also acknowledged by receiving several accolades. These included being recognised by Citibank for US dollar (USD) fund transfer services and Barclays Bank for Great British Pound remittance services. The bank was also honored at the Asian Banker Technology Innovation Awards for customer relationship management.

Deepening our Relationships with the Private and Government Sector

The government and private sector appreciated the Bank's efforts in developing tailor-made solutions that addressed their specific needs. This included the launch of several digital banking services such as business-to-business integrations, diversifying the Bank's merchant acquiring business and a comprehensive and seamless Corporate Internet Banking portal. This solidified our relationship with the public and private sectors and was a testament to our innovation capabilities and leading edge competitive advantage.

Supporting Small & Medium Enterprises (SME)

NBO has been evolving with the country's SME sector, developing a deep understanding of the business owner segment and their intricate needs. Today, the Bank has become the partner of choice to over 17,000 of Oman's budding entrepreneurs, providing them with access to both finance and guidance. The services and products offered are carefully tailored and relationship-driven to give young business leaders the means to pursue their aspirations.

Ahead of the game, NBO has always understood the fundamental role that entrepreneurs play in creating strong and diversified economies and as a result, was one of the first banks to set-up an independent department to cater to SME requirements in early 2012. Over the years, the Bank's products and services have expanded to not only include seamless financial solutions but also cross-border banking facilities between Oman and the UAE as well as training and mentorship programmes. NBO has been guiding and advising SMEs and as a result, has helped several entrepreneurs go from micro to medium and large sized enterprises.

The Business Banking Unit has recorded a strong performance in 2017, with good growth in fee income and loans and deposits, while maintaining a sharp focus on asset quality.

Leveraging our Presence in the UAE

As the only Omani bank with presence in the UAE, NBO designed an exclusive service to simplify cross-border banking transactions between Oman and the UAE. Offering this seamless banking service allowed companies in both countries to safely and securely make instant fund transfers from their NBO accounts to any bank account in either country. The Bank's Corporate Internet Banking platform also allowed clients to view all their activities on a single dashboard, clear cheques, make deposits and withdrawals, and check their financial history.

With volatile market conditions, falling oil prices, tight liquidity and rising NPAs, our main priority in the UAE has been on early warning accounts management. We took the necessary measures to strengthen our internal operational controls to enhance asset quality.

Islamic Banking

With the vision to become the leading provider of Islamic financial services in Oman, we decided to differentiate our offering by launching Muzn Privilege Banking. This proposition offered a variety of customized services and Islamic banking financial products along with additional benefits such as a dedicated relationship manager, global access to more than 500 airport lounges, over 900 offers provided by various retailers across the Sultanate and preferential profit rates.

Management Discussion and Analysis Report 2017

Risk Management

Prudent risk management was an overarching theme for the Bank in 2017, against a backdrop of a challenging market. The bank sets a risk appetite based on current and anticipated exposures, and views on the evolution of markets and the economy in normal and stressed conditions.

Therefore, dedicated early warning mechanisms were put in place to actively monitor, analyse, act on and prevent any adverse risk. Our ambition is to consistently rank in the top quartile performers in terms of Return on Assets in the GCC.

Driving Operational Efficiencies

To deliver a consistently superior banking experience across all our customer touch-points, we developed programmes to further build on NBO's strong foundations. In 2017, we continued to roll-out the internal lean management programme 'Al Jawda' that introduced continuous process improvements through the elimination of waste process management with a greater focus on quality.

We also made substantial enhancements to our Trade Finance operations to deliver a superior banking experience by restructuring our existing processes, up-skilling our employees and re-aligning our business model to cater to our customers' evolving requirements.

Developing a First Class Workforce

We are committed to creating an environment in which our colleagues feel enabled and engaged to fulfil their full potential. To support this objective, we continue to introduce internal talent management programmes that would not only attract talent to the Bank but also retain them.

Fostering a high performance and values-based culture is critical to our success as an organization, and we continue to build initiatives that drive the right behaviors that underpin our values. Our staff engagement survey results have shown a significant increase in engagement levels across the Bank. We also continue

to run internal engagement programmes such as the quarterly 'Meet & Greet the Chairperson' initiative that gives employees the opportunity to interact with members of the Bank's Senior Management Team.

Attracting and developing local talent continues to be a priority for us a bank as we look to support Oman's wider socio-economic objectives, and we are delighted to have increased our Omanisation ratio to 92.55 percent in 2017.

Positioning Ourselves for Growth while Delivering a Positive Impact

Every year, NBO strives to make a positive impact across communities in the Sultanate, and in 2017 we continued to deliver on that promise. Our programmes and events were diverse, impactful and unique with an aim to build a brighter future for the country.

One recurring theme throughout 2017 was our drive to 'inspire innovation'. Underscoring our commitment to the next generation of innovators, we hosted the Sultanate's biggest 'Hackathon' at our new head office in Athaibah, Muscat. Over 300 students, start-ups, and entrepreneurs across the country competed to produce the next big tech-driven idea that will shape the future of banking. One of the highlights of the event was a family of Omani innovators from Rustaq, who won the hearts and minds of the audience with their 'smart bank' concept, an 'internet of things' notion that enables banks to efficiently and remotely control their operations in a more sustainable manner; the idea was inspired by the family's seven-year old son.

We also reaffirmed our commitment to the wider community, and the youth population in particular, by collaborating with Golf Oman. This entailed teaching students between the ages of 4 to 18 golf through a series of engaging workshops and hands-on lessons.

In 2017, we continued to promote the Sultanate as a leading golfing destination. Our support of the NBO Golf Classic Grand Final for the fourth consecutive year has cemented Oman as a major hub for golf, ultimately contributing to the diversification strategy of the country by creating new opportunities in the hospitality and tourism sectors.

During the Holy Month, NBO launched its Shahr Al Attaa initiative. Staff from all departments of the bank distributed food hampers and clothes to underprivileged families across the Sultanate. The purpose of the programme was to ensure that as many families as possible had the means to celebrate the special month. Each hamper was personally delivered by NBO volunteers in order to connect with the families, strengthen bonds and build bridges with the local community.

In Q4, we welcomed women from across the Sultanate for a special event celebrating Omani Women's Day. The occasion was the latest edition of Women@NBO, which is an ongoing initiative that inspires women to achieve personal and professional success. This event was organised to empower, inspire and aspire women of all walks of life. This year, we were graced by the presence of Dr. Muna Mahfoudh, the first Radio and TV presenter in Oman, Aisha Al Hajri, Co-founder of Salma's Chocolates, and Ahlam Al Maqbali, an entrepreneur who built a successful platform to help women grow their businesses.

In line with CBO circular BDD/CBS/CB/5723, NBO has always been proactive in ensuring that all its customers have access to financial products and services that meet their needs, across the distribution network. This includes adopting the latest technology to extend banking services to customers anywhere, anytime from the comfort of their home, priority queuing services for people with disability as well as a clear policy and framework to ensure all customers are treated fairly and equally.

NBO understands and embraces its role in Oman's economy and society. Whether customers are accessing its banking products and services, or interacting with one of its many CSR initiatives, the Bank strives to create a nurturing internal and external culture by leaving a positive imprint on the people of Oman.

Looking Ahead

The progress we have made positions us well to achieve our vision for the future. We have extraordinary capabilities with our people and our technology. In our continuous endeavor to create and deliver value to our stakeholders, we draw on the strength of our brand, our strong, well-funded and diversified balance sheet, our customer-centric business model, and our polished track record of innovation to deliver the best to our customers. It is the shared values, skills and expertise of our people that drive the way we interact with customers, with each other, and with the community at large.

We have developed a focused segmentation model and identified three core value propositions that will truly ingrain NBO in the minds of our customers and we will continue to focus on segments where we can deliver a differentiated experience and generate sustainable returns.

We have set a bold aspiration to build new sustainable revenue lines and achieve solid and sustainable growth. Achieving these targets, requires a fundamental shift in our business model away from Traditional Loan Income to a sustainable fee generating business. Therefore, our future banking business model is centered on being a lifestyle partner to our clients and providing innovative solutions that will make NBO 'future ready'.

Corporate Governance Report 2017

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PR No. HMH/15/2015; HMA/9/2015

REPORT OF FACTUAL FINDINGS

TO THE SHAREHOLDERS OF NATIONAL BANK OF OMAN SAOG

We have performed the procedures agreed with you pursuant to the Capital Market Authority's (CMA) circular no. E/4/2015, dated 22 July 2015, with respect to the Board of Directors' corporate governance report of National Bank of Oman SAOG (the "Bank") as at and for the year ended 31 December 2017 and its application of the corporate governance practices in accordance with amendments to CMA Code of Corporate Governance issued under circular no. E/10/2016 dated 1 December 2016 (collectively the "Code"). Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon procedures engagements. The procedures were performed solely to assist you in evaluating the extent of the Bank's compliance with the Code as issued by the CMA and are summarised as follows:

1) We obtained the corporate governance report (the "report") issued by the Board of Directors and checked that the report of the Bank includes as a minimum, all items suggested by the CMA to be covered by the report as detailed in the Annexure 3 of the Code by comparing the report with such suggested content in Annexure 3; and

2) We obtained the details regarding areas of non-compliance with the Code identified by the Bank's Board of Directors for the year ended 31 December 2017. The Bank's Board of Directors has not identified any areas of non-compliance with the Code.

We have no exceptions to report in respect of the procedures performed.

Because the above procedures do not constitute either an audit or a review made in accordance with International Standards on Auditing or International Standards on Review Engagements, we do not express any assurance on the corporate governance report.

Had we performed additional procedures or had we performed an audit or review of the corporate governance report in accordance with International Standards on Auditing or International Standards on Review Engagements, other matters might have come to our attention that would have been reported to you.

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose. This report relates only to the accompanying corporate governance report of National Bank of Oman SAOG to be included in its annual report for the year ended 31 December 2017 and does not extend to any financial statements of National Bank of Oman SAOG, taken as a whole.

Ernst & Young LLC

Muscat
10 March 2018

ERNST & YOUNG LLC
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Corporate Governance Report - 2017

Corporate governance deals with the way companies are managed and led, defines the roles of the Directors and formalizes the internal control process within the institution.

The Board of Directors of National Bank of Oman (the Bank) supports the fostering of a healthy governance culture at the Bank. Accordingly, the Board and its Committees continuously evaluate and improve their governance practices, policies and procedures and confirm that the Bank applies the principles set out in the Capital Market Authority (the "CMA") Code of Corporate Governance (the "Code") as amended for Muscat Securities Market (the "MSM") Listed Companies and the regulations for Corporate Governance of Banking and Financial Institutions issued by the Central Bank of Oman (the "CBO"). In 2016, a new Code of Corporate Governance ("Code") issued by the Capital Market Authority (CMA) came into effect on July 22nd. The Board and Senior Management have worked together to ensure the prompt and proper implementation of the principles stipulated in the Code. Memberships and Terms of Reference of some of the Board committees were amended accordingly. Many existing policies have been revised and some new policies were established to be in line with the new Principles of the Code.

In accordance with the directives of the Code promulgated by the CMA, the Bank continues to include a separate report on the Bank's Corporate Governance which is duly certified by the statutory auditors within the Annual Report.

Board of Directors

The Board of Directors is responsible for the overall direction, supervision and control of the Bank. Specific responsibilities of the Board include approving the business objectives of the Bank, approving strategies and policies which need to be pursued in order to achieve these objectives, and reviewing on an on-going basis the performance of the Bank in relation to its stated objectives as well as adherence to policies.

Appointment of Directors

The Board is comprised of 11 members who were elected by the shareholders in March 2017 for a period of three years. The current term of all the Directors will expire at the end of March 2020.

Process of nomination of the Directors

The nomination of the Directors is as per Articles 29 to 34 of the Bank's Articles of Association and also in accordance with CBO, CMA, Ministry of Commerce and Industry ("MOCI") and MSM regulations. The ENRC reviews the appropriate skills and characters required of the Board Members and recommends suitable names to the shareholders for election. Shareholders retain the power to elect any candidate to the Board irrespective of whether this candidate is recommended by the Board or otherwise.

Characteristics and core competency of the Board

Members of the Board and its committees bring appropriate knowledge and experience as well as independent judgment to Board meetings and in passing resolutions. The Board collectively possesses professional knowledge, business expertise, industry knowledge and financial awareness to carry out its oversight responsibilities over the Executive and Senior Management of the Bank.

Information given to the Board

The Directors are given appropriate and timely information so that they can maintain full and effective control over strategic, financial, operational, risk, compliance and governance issues. The information provided to the Board is as per the guidelines provided in the Code.

On appointment, each Director receives information about the Bank through an induction pack and is advised of the legal, regulatory and other obligations devolving upon a Director of listed companies.

Composition of the Board

No Director is a member of the Board of more than four public joint stock companies or banks whose principal place of business is in the Sultanate of Oman, or is a Chairman of more than two such companies.

The following tables show the position of each of the current Board members in line with the Code's requirements:

Table (1)

Name of Director	Representing	Category of the Director*
Sayyidah Rawan Ahmed Al Said – Chairperson	Herself	NEX-IND
Sheikh Abdulla Bin Ali Bin Jabor Al Thani – Deputy Chairman	The Commercial Bank - Equity Investor	NEX-NIND
H.E. Abdul Rahman Al Attiyah - Director	Himself	NEX-NIND
Ms. Amal Bahwan – Director	Suhail Bahwan Group Holding- Equity Investor	NEX-NIND
Mr. Hamad Mohammed Al Wahaibi – Director	Himself	NEX-IND
Mr. Mohd Ismail Mandani Al Emadi – Director	Himself	NEX-NIND
Mr. Rahul Kar – Director	Himself	NEX-IND
Mr. Fahad Abdul Rahman Badar – Director	Himself	NEX-NIND
Mr. Ghassan Khamis Ali Al-Hashar – Director	Public Authority for Social Insurance - Equity Investor	NEX-IND
Mrs. Najat Ali Al Lawatia – Director	Civil Service Pension Fund - Equity Investor	NEX-NIND
Mr. Rashid A Saadi	Himself	NEX-IND

*NEX: Non-Executive Director, IND: Independent, NIND: Non Independent

As per the CMA guidelines, five Board members are currently considered as independent (which is more than one third of the Board) as per the required minimum number of Independent Directors as stated in the Bank's Articles of Association and the Commercial Companies Law.

Table (2)

Name of the Director	Other Board Committees Membership*	No. of other S.A.O.G Boards membership	No. of Board meetings attended	Attended last AGM on 26th March 2017
Sayyidah Rawan Ahmed Al Said - Chairperson	ENRC	1	7	Yes
Sheikh Abdulla Bin Ali Bin Jabor Al Thani – Deputy Chairman	ENRC	NIL	8	Yes
H.E Abdul Rahman Hamad Al Attiyah	BRC	NIL	8 (1 by proxy)	Yes
Ms. Amal Suhail Bahwan	ENRC, BRC	3	7	Yes
Mr. Mohd Ismail Mandani Al Emadi	BRC, BAC	NIL	7 (1 by proxy)	Yes
Mr. Hamad Mohammed Al Wahaibi	CCB, ENRC	3	6	Yes
Mr. Rahul Kar	BAC	3	8 (1 by proxy)	Yes
Mr. Fahad Badar	CCB	NIL	8	Yes
Mr. Ghassan Al-Hashar (Elected on March 26th 2017)	BAC, BRC	0	6	No
Mrs. Najat Al Lawatia (Elected on March 26th 2017)	CCB	1	6	No
Mr. Rashid Al Saadi (Appointed on August 17th 2017)	BAC, CCB	3	2	No
Mr. Mohammed Mahfoodh Al Ardhi – Ex-Chairman (Resigned on April 9th 2017)	ENRC	N/A	3	Yes
Dr. Faisal Al Farsi (Left the Board on March 26th 2017 after the AGM)	BAC, BRC	N/A	2	No
Mr. Saif Al Yazidi (Left the Board on March 26th 2017 after the AGM)	CCB	N/A	0	No

*BAC: Board Audit Committee, CCB: Credit Committee of the Board, BRC: Board Risk Committee, ENRC: Executive, Nomination and Remuneration Committee.

Number and dates of Board meetings

National Bank of Oman held eight Board meetings during 2017. They were on January 4th, January 25th March 26th, March 29th, April 26th, July 26th, October 29th and December 13th 2017.

The maximum interval between two meetings was 96 days. This is in compliance with the current regulations, which require meetings to be held within a maximum time gap of four months.

Corporate Governance Report 2017

Remuneration to Board and Top Management

The sum of the benefits (e.g. salaries, perquisites, bonuses, gratuity, pension, etc.) paid to the top 5 senior managers of the Bank in 2017 is RO 1,704,979.

Staff service contracts are two years for expatriate officers and determined by the prevailing labor laws for Omanis. The notice period is between two and six months for the existing contracts.

As all members of the Board are Non-Executive Directors, accordingly no fixed remuneration or performance linked incentives are applicable. The Non-Executive Directors are paid sitting fees and reimbursement of expenses for attending the Board and Committee meetings. In addition to the sitting fees paid, the total remuneration for the Directors, in 2017, is RO 97,600.000 subject to the Annual General Meeting approval proposed to be held on 25th March 2018.

The details of the sitting fees paid or accrued for payment during 2017 are as follows:

Table (3)

Name of the Directors	Total fees RO	Remarks
Sayyidah Rawan Ahmed Al Said - Chairperson	8,250	
Sheikh Abdulla Bin Ali Bin Jabor Al Thani – Deputy Chairman	9,000	
H.E. Abdul Rahman Hamad Al Attiyah	7,650	
Ms. Amal Suhail Bahwan	9,450	
Mr. Mohammed Ismail Mandani Al Emadi	10,000*	
Mr. Hamad Mohammed Al Wahaibi	10,000*	
Mr. Rahul Kar	10,000*	
Mr. Fahad Badar	10,000*	
Mr. Ghassan Al-Hashar	8,100	Elected on March 26th 2017
Mrs. Najat Al Lawatia	8,700	Elected on March 26th 2017
Mr. Rashid Al Saadi	4,500	Appointed on August 17th 2017
Mr. Mohammed Mahfoodh Al Ardhi – Ex-Chairman	3,450	Resigned on April 9th 2017
Dr. Faisal Al Farsi	3,300	Left the Board on March 26th 2017 after the AGM
Mr. Saif Al Yazidi	0	Left the Board on March 26th 2017 after the AGM
Total	102,400	

*The total amount of sitting fees that can be paid to a Director during a financial year is RO 10,000 according to the current regulations.

The total training, hotel and travel expenses related to the Board Members during 2017 is RO 81,357.07.

Board Committees

As at the end of December 2017, The Board of Directors has four standing committees: Executive, Nomination and Remuneration Committee (ENRC), the Board Audit Committee (BAC), the Board Risk Committee (BRC) and the Credit Committee of the Board (CCB).

Board Audit Committee (BAC):

The BAC comprises of four members, three of which are independent and one is non-independent. The committee met seven times in 2017. The composition of the BAC and particulars of meetings attended by the members of the BAC are given in the table below:

Table (4)

Name	Position	Meetings attended	Remarks
Mr. Rahul Kar	Chairperson	7	
Mr. Mohd Ismail Mandani Al-Emadi	Member	5	
Mr. Ghassan Khamis Al Hashar	Member	3	Joined the committee on 26/03/2017 after the AGM
Mr. Rashid Al-Saadi	Member	2	Joined the committee on 17/08/2017 after the AGM
Sayyidah Rawan Ahmed Al Said	Ex-Chairperson of the Committee	2	Left the committee on 26/03/2017 after the AGM
Dr. Faisal Abdullah Al Farsi	Ex-Member	2	Left the committee on 26/03/2017 after the AGM

The Audit Committee Charter which specifies the responsibility and authority of the Board Audit Committee is approved annually by the Board.

The responsibilities of the Committee as specified in the Audit Committee Charter include but are not limited to:

- Provide recommendation to the Board of Directors for putting before the Annual General Meeting for the appointment and removal of external auditors as well as specifying the fees considering the independence of such auditors.
- Discuss with the external auditors their audit plan and the results of their audit including whether they have had full access to all relevant documents.
- Approve non-audit services awarded to the external auditors (statutory) prior to commencing engagements and ensure that their independence is not compromised in any manner, further such engagements comply with Capital Market Authority Oman (CMA) regulations.
- Review and approve the Audit Division's Charter, annual budget, staffing and their compensation (including bonus) and organization structure of audit division.
- Review and approve the appointment, promotion, replacement, reassignment or dismissal of the Chief Internal Auditor of the bank.
- Review and discuss and approve the overall scope of the annual internal audit plan with the Chief Internal Auditor including the adequacy of the individual audits, staffing and their full access to all relevant documents.
- Review the effectiveness of the internal audit function, including conformance with the Institute of Internal Auditors' the Definition of Internal Auditing, Code of Ethics and the International Standards for Professional Practice of Internal Auditing
- Review and discuss with the Chief Internal Auditor, the findings of critical importance arising from the internal audits carried out in the period between meetings.
- Review management's responsiveness to internal audit findings and recommendations and assess internal audit effectiveness.
- Review and discuss with the management, internal auditors and external auditors the adequacy and effectiveness of the internal control system, including information technology security, accounting and financial controls and the Bank's system to monitor and manage business risk, and its legal and ethical compliance programs. They may appoint external consultants if deemed necessary.

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- Submit the minutes of all meetings of the Audit Committee to or discuss the matters discussed at each committee meeting with the Board of Directors of the Bank.
- Periodically assess and report to the Board of Directors, its own performance against its annual work plan, considering the effective use of committee time, responsiveness to the Board-approved charter, and the effectiveness of relationships and communications with management, auditors and the full Board.
- Review and reassess the charter at least annually and obtain the approval of the Board of Directors.
- Meet with external and internal auditors separately, at least once per annum without the management, to hear their views and to consult them vis-à-vis enhancing the level of corporate governance and compliance.
- Serve as a channel of communication between external auditors and the Board and also internal auditors and the Board.
- Oversee the financial reporting process on behalf of the Board including review of the annual and quarterly financial statements before publication, review of qualifications/ reservations in the draft financial statements and discussion of the accounting principles. In particular, any changes in the accounting policies, principles and accounting estimates in comparison to the previous year any adoption of new accounting policy, any departure from International Financial Reporting Standards (IFRS) and non-compliance with the disclosure requirements prescribed by regulatory authorities such as CBO, CMA etc., should be critically reviewed and discussed with the management and auditors.
- Ensure that management of the Bank has put in place an appropriate system for the adoption of relevant accounting policies and principles leading to the true and fairness of the financial statements. Against this system, the committee should review the financial statements for any content of fictitious or fraudulent nature.
- Review the details of all proposed related party transactions in line with the Bank's policy (complies with the CMA code of Corporate Governance) and provide appropriate recommendation to the Board.
- Periodically review internal audit findings on the 'restructured' loans upgraded to 'regular' category for information and provide appropriate directions thereon to the management.

Credit Committee of the Board (CCB):

The CCB comprises of four members. The committee has met ten times during 2017. The names of the members, their positions and their meeting attendance appear in the table below:

Table (5)

Name	Position	Meetings attended	Remarks
Mr. Hamad Al Wahaibi	Chairperson	10	
Mr. Fahad Badar	Member	9	
Mrs. Najat Ali Al Lawatia	Member	7	Joined the committee on 26/03/2017 after the AGM
Mr. Rashid Al-Saadi	Member	3	Joined the committee on 17/08/2017
Mr. Rahul Kar	Ex-Member	3	Left the committee on 26/03/2017 after the AGM
Mr. Saif Said Al Yazidi	Ex-Member	Nil	Left the committee on 26/03/2017 after the AGM

The CCB's main responsibilities include but are not limited to:

- Approve and renew credit transactions up to the maximum legal limits of the Bank including underwriting exposures and sell down targets.
- Review reports of risk assets covering bank wide portfolio trends including higher risk assets, exposures as well as the other reports at least every quarter.

Board Risk Committee (BRC):

The Board Risk Committee comprises of four members. The committee has met four times during the year 2017. The major responsibilities of the committee include risk identification and review, risk policy, risk limits and risk management and monitoring, review management of recovery strategies of problem loans and adequacy of provisioning.
The names of the members of the BRC, their positions and their meeting attendance appear in the table below:

Table (6)

Name	Position	Meetings attended	Remarks
Mr. Mohd Ismail Mandani Al-Emadi	Chairperson	4	
H.E. Abdul Rahman Hamad Al-Attiyah	Member	4	
Ms. Amal Bahwan	Member	2	
Mr. Ghassan Khamis Al Hashar	Member	3	Joined the committee on 26/03/2017 after the AGM
Dr. Faisal Al Farsi	Ex-Member	1	Left the committee on 26/03/2017 after the AGM

The responsibilities of the Committee as specified in the Terms of Reference which includes but is not limited to:

- The Committee sets the policy on all risk issues and maintains oversight of all Bank risks through the Management Risk Committee (MRC). More specifically the key responsibilities of the Committee are:

1. Approval of new policies of the Bank and periodic review of existing policies.
2. To establish an appropriate Credit Risk Environment.
3. To develop appropriate Operational Risk Management.
4. To consider the strategic Risks facing the Bank and refer suggestions for mitigating such risks to the full Board.
5. To maintain an oversight on Interest Rate Risk, the B ank's balance-sheet and income risks.
6. Management of Liquidity Risk.
7. Management of all other Market Risks including Foreign Exchange.
8. Approval of credit loss write-offs which are over the limits prescribed for the Management.
9. Management of People Risk.
10. Overseeing information security risk and business continuity risk.
11. Review management of recovery strategies of problem loans and adequacy of provisioning.
12. Formulation and review of the Key Risk Appetites of the Bank.

- **Specific Responsibilities of the Committee include the following:**

1. Recommend the Risk Strategy of the Bank, including but not limited to credit strategy, for Board approval.
2. Recommend the Risk Charter of the Bank for Board approval, review the Charter annually.
3. Set a high-level bank-wide risk policy framework within the segments of credit, market, operational, reputational, legal, strategic and accounting risks.
4. Establish risk tolerance levels and portfolio limits, including limits associated with industry sector, geography, asset quality and others, as appropriate.
5. Monitor the enterprise-wide dashboard of risk through the MRC.
6. Review and assess the performance of MRC and the Risk Group in monitoring and controlling all risk to ensure that risk strategies and policies approved by the Board are adhered to and implemented.

7. Direct oversight over Regulatory and Legal Compliance through the MRC.
8. Regularly review stress scenarios to measure the impact of unusual market conditions and monitor variance between the actual volatility in portfolio values and that predicted by the risk measures.
9. Monitor compliance of various risk parameters by business lines.
10. Approval and annual review of all asset and liability product strategies to include but not be restricted to, all retail lending products and deposit products, treasury and investment products and any other non-standard products relating to corporate banking.
11. Direct oversight over specific credit policy issues including but not limited to:
    - Credit rating models, country limits, concentration issues, loan review mechanism and findings classification policy for loans and provisioning policy.
    - Approval of new product strategies/ initiatives having credit implications for the Bank.
    - Review of appropriateness of credit authorities and delegations to management.
    - Periodic review of the Bank's Credit Risk Rating methodology and appropriateness of risk ratings.
12. Endorse the ICAAP document for the approval of the Board.
13. Review the Corporate Governance Report.

Executive, Nomination & Remuneration Committee of the Board (ENRC)

The ENRC comprises of four members and met five times during the year 2017.

The names of the ENRC members, their positions and their meeting attendance appear in the table below:

Table (7)

Name	Position	Meetings attended	Remarks
Sayyidah Rawan Ahmed Al Said	Chairperson	3	Joined the committee on 26/03/2017 after the AGM
Sheikh Abdulla Bin Ali Bin Jabor Al Thani – Deputy Chairman	Member	5	
Ms. Amal Suhail Bahwan	Member	5	
Mr. Hamad Mohammed AL Wahaibi	Member	4	
Mr. Mohammed Mahfoodh Al Ardhi	Ex- Chairperson	2	Resigned from the Board on April 9th 2017

The main responsibilities of the ENRC as specified in the Terms of Reference include but are not limited to:

- Develop the long term strategy of the Bank based on economic and market conditions and the Board's vision and recommend it for Board approval.
- Review the Bank's overall strategy and monitor implementation and execution.
- Review the performance of the Bank against approved strategy and budgets.
- Review and recommend for Board approval the Bank's annual Budgets and Business Plans including all Operating and Capital Expenditure budgets of the Bank in line with the long term strategy and changes in economical, market and regulatory environments.
- Review reports and analysis of the Bank's financial and operating performance, and evaluate key performance indicators against their accompanying strategies.
- Review the performance of the Investment Banking function including all investments reports.
- Review and recommend to the Board the Bank's proposals for Capital Raising Plan.

- Review and approve the Banks Dividend Policy and recommend to the Board the proposed dividend payout.
- Review and approve NBO's brand vision.
- Review and approve the Bank's Human Resources Manual and Policy and the Bank's Compensation Policy and Bonus Plan.
- Be responsible for setting the Bank's remuneration framework for management and staff as per the Bank's Compensation Policy and Bonus Plan and ensure its proper implementation.
- Review prevailing compensation and benefits and ensure consistency with market trends as per the Bank's Compensation Policy and Bonus Plan in accordance with regulatory guidelines.
- Review, approve and amend policies related to employee reward and performance related incentive plans and assume the function and responsibilities of the Remuneration Committee as specified in the Bank's Compensation Policy as approved by the Board.
- Handle appointment and movement of key executives in the Bank from the reward level Assistant General Manager (AGM) and above.
- Review and approve major changes in the Bank's organizational structure at the level of Divisional Heads and above.
- Have specific responsibility to recommend for Board approval, and to review and update as necessary, a general strategy and policies for the acquisition, ownership and development of the Bank's properties.
- Approve the acquisition and sale of any property required for the business of the Bank.
- Approve the appointment of construction companies and consultants for the Bank's Head Office, and agree the terms of any construction contract (including any variation order), consultancy or property or facilities management contract relating to any property owned by the Bank.
- Shall oversee the performance and implementation of any property-related projects.
- Propose the annual CSR and Sustainability budget to the Board, which shall submit the same to the shareholders in their Annual General Meeting for approval.
- Identify methods of payment for CSR and Sustainability initiatives.
- Submit a report at the end of the year to the AGM for ratification of amounts paid to CSR and Sustainability initiatives.
- Adopt a transparent method in preparing the Nomination Policy targeting directors of high competence and caliber, without prejudice to the right of any of the shareholders to stand for election or to nominate whoever they see fit.
- Exert the best efforts to the assist the Bank in formulating clear, credible and accessible policies to inform the shareholders about Director's and executives' remuneration.
- Prepare detailed job descriptions of the role and responsibilities for Directors including the Chairperson. This will facilitate the orientation of the Directors towards their tasks and roles and appraise their performance.
- Look for and nominate qualified persons to act as interim directors on the Board in the event a seat becomes vacant.

Corporate Governance Report 2017

Board Members Profiles

Sayyida Rawan Ahmed Al Said, Chairperson

Chairperson of the ENRC. Dr. Sayyida Rawan Ahmed Al Said is the CEO of Takaful Oman SAOG. Prior to joining Takaful Oman, she was the Managing Director and CEO of ONIC Holding Corporation. Before moving to the Private Sector, Rawan was the Deputy CEO-Investment for the State General Reserve Fund of Oman, leading the execution of many mega investments internationally. She has almost 30 years of experience in the financial industry, 20 of which are in the Public sector.

She has been a member on the Board of a number of reputed Companies and Financial Institutions in Public and private sector in Oman and in the region. Chairperson in National Bank of Oman, Deputy Chairperson in Oman Oil Marketing Company, Board Member of Oman National Investments Development Company ONIDCO (Tanmia). Public companies she was the Board Member of Oman Oil Company SOAC and its Audit Committee. Chairperson of its Equity and GCC Funds. Board Member in International General Insurance (IGI) Jordan, and National Finance House (NFH), Bahrain. Deputy Chairperson of Orix Finance, National Life & General Insurance Company SAOC (NLIG) and Al Ahlia Insurance.

She is also a Member on the Investment Committee of the Public Authority for Social Insurance, Board Member in Public Authority for the SME Development (Riyada). Chairperson of Al Kawther Fund (Islamic Compliant Fund) and a Member of the Investment Committee of Orphans & Incapacitated Funds in the Ministry of Justice. She has been recently appointed as a Board member of the Sultan Qaboos University Council.

Sayyida Rawan remains to be the First and the only Female who holds a CEO position in a public listed company in Oman.

In 2011, She was bestowed the Business Professional (BizPro) Leader Award. In 2012, was ranked 14th in Forbes Middle East for the 'Most Powerful Arab Business Women in Listed Companies'. In 2014, Rawan was named among the Best Chief Executives in the region by Trend in collaboration with INSEAD (The Business School for the World). Also she was Awarded Hall of Fame by MARA Excellence Awards. In 2015, she was honored with two prestigious Awards; Asian Women Leadership of the Year from World Leadership Congress and in MENA and Business Leader of the year from the Middle East Accountancy and Finance Excellency Awards 2015. In 2016 she was honored with Honorary Doctorate Degree from Commonwealth University in UK and she was awarded as the Best Takaful CEO from Global Business Outlook, UK. In 2017 she won the best Takaful CEO-Oman, International Finance, London. Dr. Rawan ranked 3rd in Oman for Forbes the Top 100 most powerful Arab Businesswomen 2017.

Dr. Sayyida Rawan, has an MSc in Economics &Finance from Loughborough University UK. She also holds a Post Graduate Diploma in Investment Analysis from Stirling University UK, and BA in Economics & Political Science from the American University in Cairo (AUC).

H.E. Sheikh Abdulla Bin Ali Bin Jabor Al Thani, Deputy Chairman

Member of the Executive, Nomination and Remuneration Committee (ENRC).

H.E. Sheikh Abdulla bin Ali bin Jabor Al Thani has been a Director of the Bank since July 2005 and serves as a member of the Board Executive, Nomination and Remuneration Committee (ENRC). His Excellency is the Chairman of The Commercial Bank (P.S.Q.C.) in Qatar, a member of the Board of Directors for United Arab Bank, P.J.S.C. in UAE and is the Owner of Vista Trading Company (Qatar), a Partner in Dar Al Manar (Qatar), Domopan Qatar and Integrated Intelligence Services Company (Qatar).

H.E. Sheikh Abdulla bin Ali bin Jabor Al Thani holds a Bachelor of Arts Degree in Social Science from Qatar University.

His Excellency Mr. Abdul Rahman Bin Hamad Al Attiyah, Director

Member of the Board Risk Committee (BRC).

His Excellency Abdul Rahman Bin Hamad Al Attiyah has been a Director of the Bank since November 2014. He serves as a member of the Board Risk Committee (BRC) and is a member of the Board of The Commercial Bank (P.S.Q.C.) since March 2014. He began his career in 1972 at Qatar's Ministry of Foreign Affairs and has served as Qatar's Ambassador in Geneva, Saudi Arabia, France, Italy, Greece, Switzerland, Yemen, and Djibouti. He also served as a permanent representative to the United Nations in Geneva, the Food and Agriculture Organization (FAO) in Rome, and UNESCO in Paris. He is the Minister of State of Qatar and holder of the state award of appreciation.

His Excellency Al Attiyah was the former Secretary-General of the Gulf Cooperation Council (GCC) from 2002 until 2011. He holds a Bachelor of Arts Degree in Political Science and Geography from the University of Miami, United States of America. He is the owner and Chairman of Mawten Trading in Qatar and Vice President of the Board of Trustees of the Arab Thought Forum – Amman, Jordan.

Ms. Amal Suhail Bahwan, Director

Member of the Executive, Nomination and Remuneration Committee (ENRC) and the Board Risk Committee (BRC).

Ms. Amal Suhail Bahwan is the Vice Chairperson of Suhail Bahwan Group Holding LLC. She has extensive experience in managing companies across the Bahwan Group.

She is also the Chairperson of Oman Ceramics SAOG, Director and Executive Committee member of National Pharmaceutical Industries SAOG and Director of Oman Oil Marketing Co SAOG.

Ms. Amal has a Bachelor's degree in Education and a Master's degree in Administration from the Sultan Qaboos University.

Corporate Governance Report 2017

Board Members Profiles

Mr. Hamad Mohammad Hamood Al Wahaibi, Director

Chairperson of the Credit Committee of the Board (CCB) and member of the Board Executive, Nomination and Remuneration Committee (ENRC).

Mr. Hamad Mohammed Al Wahaibi has been a Director of the Bank since March 2014. He has 18 years of experience in the GCC. He has been a director of investment with the Ministry of Defense Pension Fund for the past five years. Mr. Al Wahaibi is also a member of the boards of Voltamp Energy Company, Oman Cables Company and ACWA Power Company.

Mr. Al Wahaibi holds a Masters of Business Administration (MBA) degree, specializing in Finance, and he is a Chartered Financial Analyst (CFA) charter holder, as well as a Chartered Alternative Investment Analyst (CAIA) charter holder.

Mr. Mohammed Ismail Mandani Al Emadi, Director

Chairperson of the Board Risk Committee (BRC) and Member of the Board Audit Committee (BAC).

Mr. Mohammed Ismail Mandani Al Emadi has been a Director of the Bank since November 2014. He is also a member of the Board for The Commercial Bank (P.S.Q.C.) and a member of the Board of Alternatifbank A.S. (ABank), Turkey and has over 30 years of banking experience. Mr. Al Emadi has held a number of key roles at Commercial Bank until 2006, after which he served as Chief Executive Officer of Qatar Real Estate Investment Company Q.S.C. up to 2011, and also served as its Director from 2003 until 2005.

Mr. Al Emadi holds a Bachelor of Arts Degree in Business Administration and Economics from Holy Names University, California.

Mr. Rahul Kar, Director

Chairperson of the Board Audit Committee (BAC).

Mr. Rahul Kar has been a Director of the Bank since April 2016. Mr. Kar is a Chartered Accountant with over 25 years of relevant experience and is currently working as the Financial Advisor to the Chairman of Suhail Bahwan Group Holding LLC.

Mr. Rahul is also a Director and an Audit committee member of National Pharmaceutical Industries SAOG and Al Suwadi Power Co SAOG. He is also a Director and Nomination & Remuneration committee member of Oman United Insurance Company SAOG.

Mr. Fahad Badar, Director

Member of the Credit Committee of the Board (CCB).

Mr. Fahad Badar has been a Director of the Bank since May 2016. He is also a member of the Board for Alternatifbank A.S. (ABank), Turkey since September 2013 and a member of the Board for ALease, Turkey since March 2016. He is also a member of the Board for United Arab Bank, P.J.S.C. in UAE since July 2016.

Mr. Badar's career at The Commercial Bank (P.S.Q.C.) in Qatar spans over 17 years. Prior to his current role as Executive General Manager, International Banking, he held a number of key roles in International Banking, the Government and Public Sector Relations and the Wholesale Banking Divisions.

Mr. Badar holds an MBA from Durham University, UK and a Bachelor of Arts Degree in Banking & Finance from the University of Wales.

Mr Ghassan Khamis Al Hashar, Director

Member of the Board Audit Committee (BAC) and the Board Risk Committee (BRC).

Mr Al Hashar joined NBO Board as a representative of the Public Authority for Social Insurance (PASI) in March 2017. He is currently the Authority's Director of Investments. He has nearly 20 years of experience in finance and investment management, and represents PASI on the boards of numerous public and private companies. He is also the Chairman of Muscat Fund Management Body and Board Director at Oman National Investments Development Company SAOC (TANMIA).

Mr. Al Hashar holds a Master's Degree in Finance and Investment Management.

Mrs. Najat Ali Al Lawatia, Director

Member of Credit Committee of the Board (CCB).

Ms. Najat Ali Al Lawatia was elected as a Director of the Bank at the AGM in March 2017. She holds a Commerce Degree in accounting and has attended various courses in diverse fields of financial management, audit, investments etc. She is working as the Deputy Director General-Support Services with Civil Service Employees Pension Fund and has more than 20 years of relevant experience.

Ms. Najat is also a Director and Chairperson of Audit Committee of Oman Cement Company SAOG.

Mr. Rashid Bin Saif Al-Saadi, Director

Member of the Board Audit Committee (BAC) and a member of the Credit Committee of the Board (CCB).

Sheikh Rashid has been a member of the Board of Directors since August 2017, and is a renowned financial and investment banker, business executive, entrepreneur and philanthropist. Sheikh Rashid is also the CEO of TANMIA, a company that actively contributes to the Sultanate's economic development.

Sheikh Rashid holds a B.Sc. in Business Administration from Rollins College, USA. His career is marked by many significant achievements and milestones; including a twelve year stint with the Diwan of Royal Court, in addition to his involvement in various specialized committees, such as the Omanization committee, the planning and budgeting committee until his appointment as the General Manager of the Arabian Engineering Services (AES) Company.

In 2000, Sheikh Rashid was appointed CEO of TANMIA, which was setting up its Investment Fund with the Muscat Securities Market at the time. Following his appointment, the Board of Directors decided to transfer the responsibilities of managing the fund to the company directly, and two new Funds were set up subsequently; a Private Equity Fund, the GCC Investment Fund, and the Sharia Fund in 2013. In addition, Sheikh Rashid also drove direct investments into various industries, including and not limited to Real Estate Development; the company played an active role in the development of the Al Mouj Muscat Project, and in the Tourism sector, the company played a key role in setting up the Kempinski Hotel, Muscat. In the Industrial Sector the company contributed to the establishment of Octal Petrochemicals, also extending into the retail sector by partnering with Al Meera Group to set up its business in the Sultanate.

In addition to his executive responsibilities, Sheikh Rashid is the Chairman of Board of Directors of Takaful Oman SAOG and A'saffa Foods SAOG. He is also a Director on the Boards of Oman Orix leasing Company, Minerals Development Company SAOC, Muscat National Development and Investment SAOC, Almouj Muscat & Oman Hospitality Company.

Composition of the Management

The organization chart of the Bank's management includes a Chief Executive Officer (CEO) as the leader of the organization whose appointment, functions and package are determined by the Board. The General Managers are appointed to assist the CEO and to lead functional groups in the Bank. The organization chart also includes Divisional Heads of all the direct subordinates of the CEO. The following table gives details of the top eight management officers along with their positions:

Table (8)

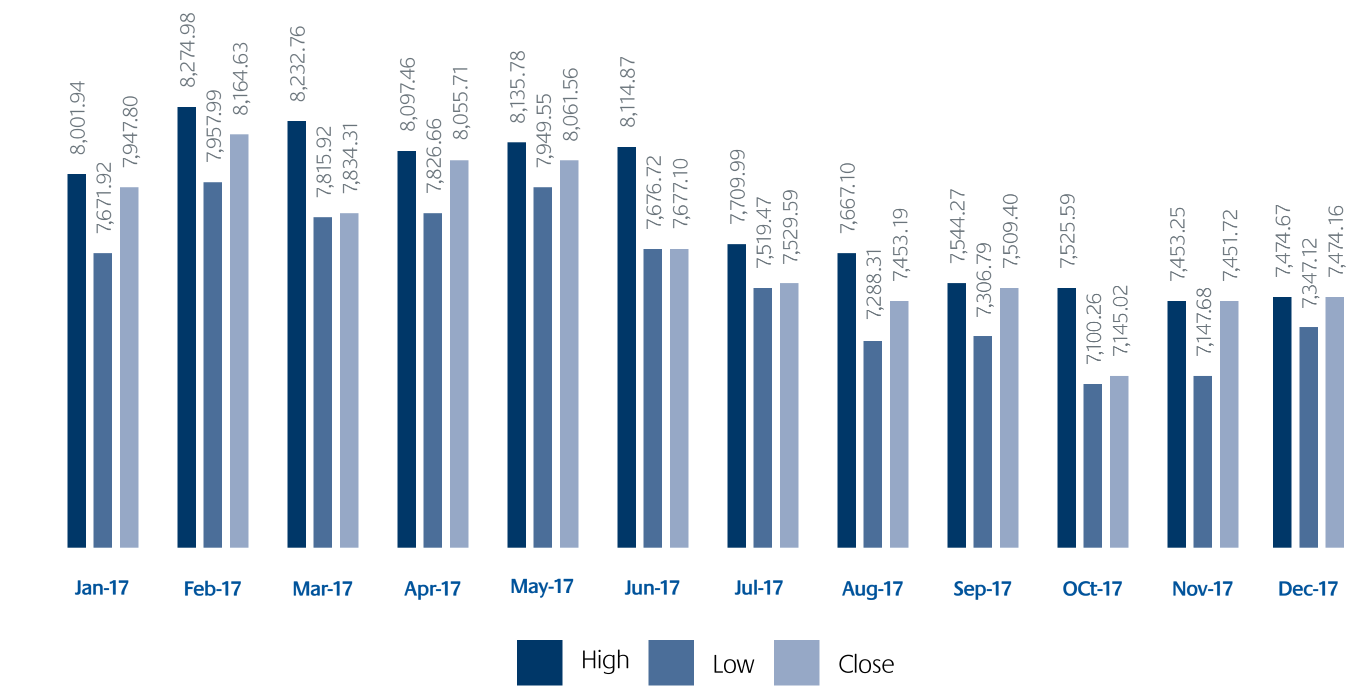
Name	Position
Ahmed Jaffer Al Musalmi	CEO
Ananthraman Venkat	GM - Chief Financial Officer
Nasser Mohammed Al Hajri	GM - Chief Corporate Services Officer
Kumar Keswani	GM – Chief Corporate Banking Officer
Nasser Salim Al Rashdi	GM - Chief Commercial Banking Officer
John Chang	GM – Chief Retail Banking Officer
Salma Salim Said Al Jaaidi	GM - Chief Risk Officer
Faizal Mohamed Eledath	GM - Chief Transformation Officer
Wasfi bin Jamshid Al Said	GM - Chief Investment Officer
Hassan Abdul Amir Shaban	GM - Chief Government Banking Officer

NBO AND MSM BANK & INVESTMENT INDEX - FY 2017

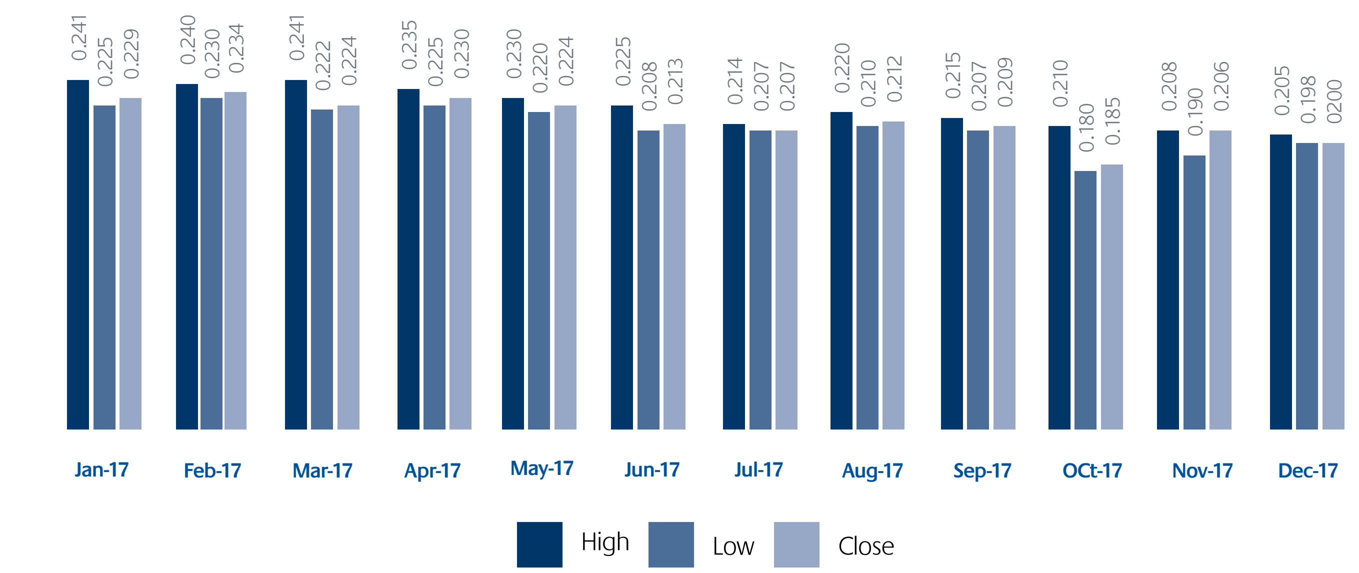
Market Price Data:

The following table shows the high, low, and average prices of the Bank's shares and compares the Bank's performance against the broad index of banks and investment companies during 2017.

Banking & Investment Index



NBO



Related Party Transactions

Details of all transactions where a Director and/or other related parties might have a potential interest are provided to the Board for their review and approval, and the interested Director neither participates in the discussions, nor do they vote on such matters.

On a half yearly basis, as of June 30th and December 31st of each financial year, the details of the Bank's related parties are produced and submitted to the Central Bank and other regulatory bodies for information and proper disclosure.

Details of all the related party transactions are provided to the shareholders as part of the financial statements submitted for approval at the Annual General Meeting along with the statement that transactions are on an arm's length and independent basis and are reasonable.

Internal Control Review

The Board attaches great importance to maintaining a strong control environment and their review has covered all controls, including financial, operational, compliance and risk management.

The Board has a collective responsibility for the establishment, maintenance and review of a system of internal controls that provides reasonable assurance of effective and efficient operations, internal financial control, and compliance with the relevant laws and regulations.

The Board has established a management structure that clearly defines roles and responsibility and reporting lines and has approved the updated policies including credit, expenditure, disclosure, corporate governance etc.

The Bank's financial position, operational and business performance is regularly reported to the Board. The actual performance achieved against budgets and prior period is reported and closely monitored.

Financial information is prepared using appropriate accounting policies that are consistently applied. Operational procedures and controls have been established to facilitate complete, accurate and timely processing of transactions and the safeguarding of assets. They are monitored through compliance with policies and procedures manuals, desk performance instructions and other circulars.

Shareholders

Communication with shareholders and investors.
The Board is committed to ensure that all material information relating to the Bank's business operations is regularly communicated to its stakeholders and members of the investment community.

The Bank has its own web site, where relevant information relating to the Bank, its products, its operations and annual and quarterly financial statements are posted. The Bank's web-site address is www.nbo.om.

- Quarterly results are published and made public. Investor Relations page / Results & Reports page

The quarterly, half-yearly, and annual results of operations of the Bank are published in leading Arabic and English newspapers in the Sultanate of Oman. After completion of the statutory audit, the annual report and the summary financial statements are sent by post to all shareholders along with the notice of the forthcoming Annual General Meeting of the Bank. Further, the shareholders are advised to contact the Bank whenever they require any updated information regarding the Bank or its operations.

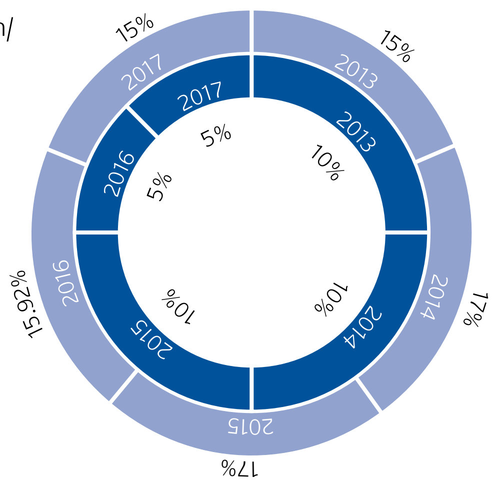
The Bank also displays official new releases on its website https://www.nbo.om/en/Pages/News/Home.aspx for the shareholders, analysts and investors.

Distribution of Dividends

The distribution of dividends to the shareholders by the Bank during the last five years appears in the chart:

Cash dividend   Bonus shares

2017 (Recommended by the Board subject to Shareholders' approval) are TBD for bonus shares and cash dividend



Corporate Governance Report 2017

Corporate Social Responsibility (CSR)

During the year 2017, the Bank distributed donations to the charitable organizations and other non-profitable organizations and participated in CSR initiatives totaling RO 250,525 which is within the budget limit approved by the Annual General Meeting held on 26th March 2017.

Details of NBO main donations and CSR initiatives during the year 2017:

1. Hackathon

We launched the first-of-its-kind Hackathon in the Sultanate to position NBO as a thought leader & to inspire Oman's youth.

Over 200 entrepreneurs, high school and college students from Oman, UAE and India participated in the competition, and had 24hrs to develop their innovative prototypes at the Bank's headquarters.

OMR 30,000

2. Women Techmakers

Under the theme "Telling Our Story", leading Omani women in entrepreneurship and technology addressed an audience of young aspiring entrepreneurs as part of a Google supported global program.

Six Omani women led the "Global Techmakers" program, which is student-organized by GUTech's Computer Science Club.The event organisers hoped to empower women in technology by highlighting prominent individuals in society and their experiences.

OMR 500/-

3. The Endangered Arab Ibex

This is a collaboration we formed with the Diwan's Office of the Conservation of the Environment.

The Arab Ibex is an endangered species that is at risk of becoming extinct.

The 3-year research study we funded traced the movements of the Arab Ibex with the objective of creating a reservation for the endangered animal.

The field research was successful and a sanctuary was created in Jibal Al Hajr to protect the Ibex from hunters.

The initiative was widely publicized on various channels (including TV, Radio, Social Media and Press) and received strong positive feedback from the community.

OMR 17,270/-

4. NBO's Scholarship Programme

In 2015 we launched a unique scholarship programme, enabling 15 students from low-income families to complete their undergraduate degrees at the top Universities in the UK.

Hakima Al Hosni was selected in 2015, she's currently completing her Undergraduate Programme at the University of Liverpool – John Moores.

Seven scholarships were awarded in 2016 & 2017 and the students are currently enrolled in various universities across the UK.

OMR 19,370 /-

5. BDI

BDI is not-for-profit organization dedicated to making a positive impact in the economies and societies of the region by promoting sound Corporate Governance practices.

A 1-year agreement was signed in October 2016 to support this initiative.

OMR 20,000/-

6. Women@NBO

The objective of the program is to inspire Women@NBO to achieve personal & professional fulfilment, and to empower them to unlock their full potential. This event will be piloted internally and then extended to the public.

Two events were held this year in February we hosted Ms. Amal Bahwan as our guest speaker & in October (to mark Omani Women's day) we hosted renowned TV presenter Dr. Muna Mahfoodh and a group of inspirational female entrepreneurs from Al Buraimi region who are breaking the glass ceiling.

In addition, to celebrate Omani Women's Day, we produced a short video by NBO's staff to inspire other women in the community to aspire for more. This video was published on all the Bank's social media channels.

OMR 11,768/-

7. Parkour Athlete

This partnership was formed between NBO and Red Bull Middle East to showcase talented youth with unique skill-sets. It was also an opportunity to unveil our New Head Office.

Dimitris Kyrsanidis is a parkour athlete from Greece, winning the 2014 and 2015 editions of Red Bull Art of Motion in Santorini brought him worldwide fame and catapulted him into the free running elite.

The video was published on all our and our partners' social media pages

OMR 0/-

8. Shahr Al Attaa

To engage with the community and support low-income families ahead of the holy month of Ramadhan, NBO's staff distributed food hampers to over 1,200 families across the Sultanate.

To complement this initiative, we also launched a unique community engagement event during Eid in collaboration with VOX cinema to grant wishes to children. The video was viewed by approximately 60,000 people

OMR 3,077/-

9. Muscat and Khareef Festival

The festivals seek to promote Tourism in the Sultanate.

We supported the Muscat Festival in January 2017 and the Khareef Festival in July 2017.

OMR 15,000/-

10. Innovation in SME Awards

To inspire the conceptualization and development of new business ideas amongst Oman's youth and to encourage the transformation of these ideas into businesses/SMEs with robust and sustainable business plans and strategies.

- Five short-listed candidates will be present their ideas to a panel of four judges in the form of a business plan on the 30th of January 2018. The winning idea will be selected based on a number of criteria, namely: The quality of the business plan/idea, its uniqueness and USP, sustainability and feasibility and its potential for success.
- A OMR10K cash prize will be awarded to the most innovative and commercially-promising business idea, a cash prize of OMR 5K will be awarded to the second place winners and a cash prize of OMR 2.5K to the 3rd place winners. The winners will join NBO's Tijarati SME mentoring program and will have access to the Bank's Academy of Excellence, NBO's network of corporate clients & will be recognized publicly.

OMR 25,000 /-

11. Mawahib Watania

As part of our commitment to support local Talent, we launched the 'Mawahib Watania' initiative as a platform for young Omanis to showcase their talent.

OMR 5,000/-

12. NBO Career Fair- Mustaqbali fi Watani

This initiative seeks to support the Nation's efforts to:

- Create employment opportunities for Omanis
- Develop and promote local talent

The objective of the initiative is to:

- Stimulate the youth's interest in potential career opportunities within the Banking industry
- Initiate a strong network of young talent
- Position NBO's Senior Leadership Team as subject matter experts and inspirational mentors
- Give students insight into the endless potential career opportunities NBO offers.

OMR 5,000/-

13. Supporting Local Talent- Ahmed Al Harthy

NBO continues to support local talent who are promoting Oman globally

OMR 10,000/-

14. Al Noor Sporting Club

NBO sponsored the Al Noor Sporting Club to purchase a distillation tank

OMR 5,000/-

15. Teacher's Day

NBO sponsored the Ministry of Educations Teacher's Day Celebrations, as a token of appreciation to the teachers who have served the community

OMR 5,000/-

16. Duqum Forum 3rd Edition

Supporting Oman's Economic growth and development by sponsoring platforms that promote thought leadership and reinforce Oman's strategicagenda.

OMR 5,000/-

17. Majan College Open Day (Invent Day)

NBO sponsored the Majan College innovation Platform (Invent Day) Where a number of students from various Colleges and Universities across Oman presented their innovative ideas to solve challenges students face on campus.

OMR 300/-

18. Redbull's Tetramerous

NBO sponsored Redbull's gaming platform

OMR 3,500/-

19. International Disabled Day Celebrations

NBO sponsored the International Disabled Day Celebration organized by the Ministry of Social Development

OMR 2,000

20. Oman Vision 2040

In line with His Majesty Sultan Qaboos bin Said's vision the Vision Oman 2040, was designed to develop a plan, and contribute to achieving and executing the plan in moving towards digitalization

OMR 7,000/-

21. Omani Women's Day Muscat Governor's Office Celebrations

NBO sponsored the Omani Women's Day Celebrations organized by the Muscat Governor's Office

OMR 500/-

22. Omani National Day Celebrations in UAE

NBO sponsored the 47th National Day Celebrations in the UAE to demonstrate Omani Pride.

OMR 5,240/-

23. Economist Roadshow

The roadshows target Sadara & Corporate clients (existing and potential).. Investment experts provide a snapshot of the local and regional economy, co-hosted by a prominent regional economist.

OMR 25,000/-

24. Volunteers' Recognition Program Talent

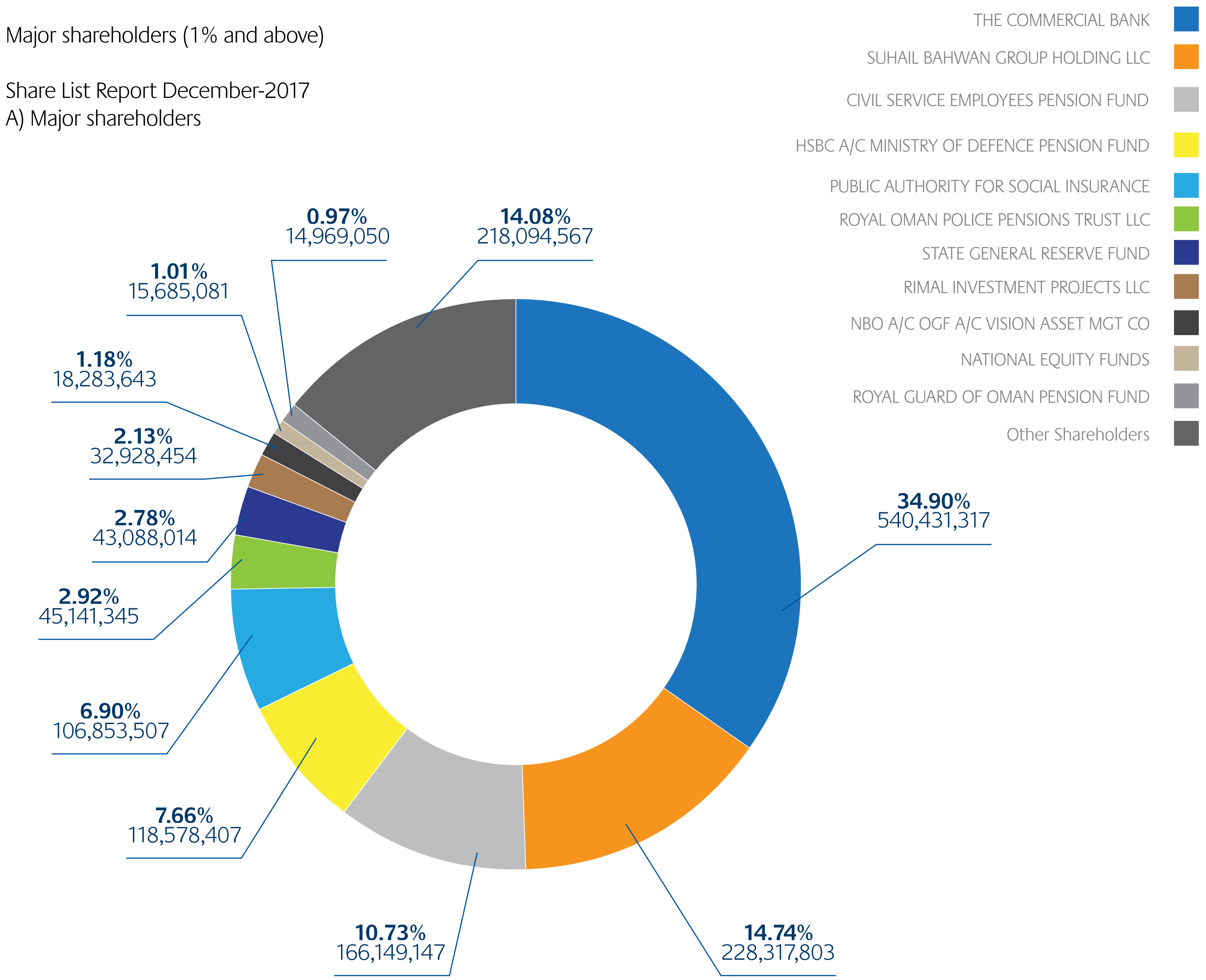
An event organized to recognize volunteers

OMR 3,000/-

Distribution of Shareholding:

Major shareholders (1% and above)

Share List Report December-2017
A) Major shareholders



The shareholding pattern as on 31 December 2017 was:

Table (9)

Number of Shares	Number of Shareholders	Total Shares	% of Capital
7,000,000 and above	16	1,361,666,945	87.93%
3,000,000 to 6,999,999	9	37,802,060	2.44%
1,500,000 to 2,999,999	21	45,554,502	2.94 %
500,000 to 1,499,999	46	39,382,225	2.54%
100,000 to 499,999	122	31,198,966	2.01%
Below 100,000	996	32,915,637	2.13%
Total	**1,210**	**1,548,520,335**	**100%**

A copy of the Management Discussion and Analysis is circulated as part of the Annual Report.

There are no Global Depository Receipts/ Warrants or any Convertible Instruments outstanding.

Details of non-compliance

Annexure 4 of the Code of Corporate Governance requires the Bank to provide details of non-compliance. This includes any penalties, strictures imposed on the Bank by the MSM / CMA or any statutory authority such as the CBO, on any matter related to capital markets, during the last three years (2015, 2016 and 2017). The Bank has identified the following amounts below paid during the last three years.

Table (10)

Particulars in OMR	2015	2016	2017
PASI	32,098	0	0
CBO	600	4,000	33,600
Total	**32,698**	**4,000**	**33,600**

Auditors

Having strong internal and external auditors is recognized by the Board as part of sound corporate governance providing an independent and continuous assessment of the adequacy of, and compliance with, the Bank's established policies and procedures.

ERNST & Young (E & Y) Profile

Profile of Statutory Auditors

EY is a global leader in assurance, tax, transaction and advisory services. EY is committed to doing its part in building a better working world. The insights and quality services which EY delivers help build trust and confidence in the capital markets and in economies the world over.

The MENA practice of EY has been operating in the region since 1923 and employs over 6,700 professionals. EY has been operating in Oman since 1974 and is a leading professional services firm in the country. EY MENA forms part of EY's EMEIA practice, with over 4,500 partners and approximately 106,079 professionals. Globally, EY operates in more than 150 countries and employs 256,500 professionals in 728 offices. Please visit ey.com for more information about EY.

EY in Oman is accredited by the Capital Market Authority (CMA) to audit joint stock companies (SAOGs). During the year 2017, EY billed an amount of RO 133,818 towards professional services rendered to the Company (RO 123,500 for audit and RO 10,318 for tax and other services).

Declaration

The Board of Directors declares its liability for preparation of the financial statements in accordance with the applicable standards and rules.

For the year under review the Board has conducted a review of the effectiveness of the Bank's internal control policies and procedures and is satisfied that the Bank's internal control are effective and that appropriate procedures are in place to implement the Code's requirements.

The Board of Directors confirms that there are no material issues that affect the continuation of the company and its ability to continue its operations during the next financial year.

Rawan Bint Ahmed Al Said
Chairperson

Basel II and III - Pillar III Report 2017

EY
Building a better working world

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muscat@om.ey.com
ey.com/mena
C.R. No. 1224013
PR No. HMH/15/2015; HMA/9/2015

REPORT ON FACTUAL FINDINGS TO THE BOARD OF DIRECTORS OF NATIONAL BANK OF OMAN SAOG (THE "BANK") IN RESPECT OF BASEL II – PILLAR III AND BASEL III RELATED DISCLOSURES OF MUZN ISLAMIC BANKING WINDOW

We have performed the procedures agreed with you and as prescribed in Title 5 of the Islamic Banking Regulatory Framework and Central Bank of Oman's (CBO) Circular No. BM 1027 dated 4 December 2007 with respect to the Basel II - Pillar III Disclosures and Basel III Disclosures (the disclosures) of Muzn Islamic Banking Window (the Islamic Window) of the Bank as at and for the year ended 31 December 2017. The disclosures were prepared by the Islamic Window's management in accordance with the related requirements set out in Title 5 of the Islamic Banking Regulatory Framework, CBO's Circular number BM 1009 dated 13 September 2006, Circular No. BM 1027 dated 4 December 2007 and Circular No. 1114 dated 17 November 2013. Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon procedures engagements. The procedures, as set out in Title 5 of Islamic Banking Regulatory Framework and Circular number BM 1027 dated 4 December 2007 were performed solely to assist you in evaluating the Islamic Window's compliance with the related disclosure requirements as set out in Title 5 of Islamic Banking Regulatory Framework, CBO's Circular number BM 1009 dated 13 September 2006 and Circular No. BM 1114 dated 17 November 2013.

We report our findings as follows:

Based on performance of the procedures detailed above, we found the disclosures free from any material misrepresentation.

Because the above procedures do not constitute either an audit or a review made in accordance with International Standards on Auditing or International Standards on Review Engagements, we do not express any assurance on the disclosures.

Had we performed additional procedures or had we performed an audit or review of the disclosures in accordance with the International Standards on Auditing or International Standards on Review Engagements, other matters might have come to our attention that would have been reported to you.

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose. This report relates only to the accompanying disclosures to be included in the Bank's annual report for the year ended 31 December 2017 and does not extend to any financial statements of the Bank or its Islamic Window, taken as a whole or to any other reports of the Bank or its Islamic Window.

Ernst & Young LLC

Muscat
10 March 2018

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ERNST & YOUNG LLC
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P.O. Box 1750 - P.C. 112, Sultanate of Oman

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CAPITAL STRUCTURE

The authorised share capital of the bank as at 31 December 2017 is 2,000,000,000 shares of RO 0.100 each.

The issued and paid up capital of the bank as at 31 December 2017 is 1,548,520,338 shares of RO 0.100 each

The bank has assigned capital for operations in UAE and Egypt, amounts equivalent to RO 34.10 million and RO 19.25 million respectively. These amounts cannot be withdrawn without the approval of the Central Banks of the respective countries. In addition, within Oman, the bank has allocated RO 13.50 million of capital towards the Islamic banking window.

The bank's consolidated capital structure as at close of 31 December 2017, based on Central Bank of Oman's (CBO) guidelines is as follows:

Elements of Capital	Amount in RO 000's
Tier I Capital **Local Banks**	
Paid-up capital	154,852
Share premium	34,465
Legal reserve	51,617
General reserve	-
Subordinated debt reserve	21,600
Stock dividend(Proposed)	7,743
Retained earnings*	135,365
Common equity Tier 1 before regulatory adjustments	**405,642**
Deduction	
Deferred tax asset	(1,558)
Cumulative fair value gains or losses on available for sale	(2,496)
Common equity Tier 1	**401,588**
Additional Tier 1 Capital	
Tier 1 Perpetual Bond	115,500
Tier I capital after all deductions	**517,088**
Tier II Capital	
General loan loss provision/General loan loss reserve	35,830
Subordinated debt (After amortization)	3,400
Total Tier II Capital	**39,230**
Total Regulatory Capital	**556,318**

*Note: Retained earnings are after deduction of RO 23.48 million towards proposed cash dividend, which is subject to Board and CBO approvals.

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CAPITAL ADEQUACY

Qualitative Disclosures:

The ultimate objectives of capital management are three fold:

- Ensure stability of the bank by holding enough capital to cover unexpected loss
- Enhance the efficiency of the bank, by increasing the risk adjusted return at various levels of aggregation (and thereby ensuring that "excess" capital is not held unnecessarily)
- Incentivize informed decision making and proactive risk management through an efficient and effective allocation of capital across the business.

The capital management plan envisaged for the bank is based on the regulatory risk capital framework of Basel II and using standardised approach for calculating the credit as well market risk and the basic indicator approach for operational risk as prescribed by CBO.

The capital management policy of the bank aims to ensure that on a risk adjusted return on capital basis (RAROC), individual lines of business are allocated an appropriate amount of capital. The RAROC model has been implemented for the entire portfolio except for Retail banking where the Central Bank of Oman has defined caps on interest rates, which are followed.

The Asset Liability Committee (ALCO) reviews and monitors capital adequacy and requirement for capital on an ongoing basis. Capital adequacy calculation is prepared and submitted for ALCO's review every month. Various stress scenarios, taking into account the earning volatility, credit and market risk impact along with capital allocation by line of business is reviewed in this forum.

Qualitative Disclosures:

A set of triggers is followed as part of the capital management so as to provide the bank with an early warning system in terms of its level of capital, to enable it to take suitable measures at an early stage to prevent capital falling below acceptable limits.

The Bank prepares ICAAP (Internal Capital Adequacy Assessment Process) document in line with Basel II guidelines to evaluate all Enterprise-wide Risks that are not fully captured in the Pillar I Risks. This document addresses through objective and subjective evaluation, the adequacy of capital after considering the impact of additional risks, such as, Residual Credit Risk, Residual Credit Risk Mitigation (CRM) Risk, Residual Credit Risk - Equity, Residual Market Risk - Currency, Credit Concentration Risk, Interest Rate Risk in Banking Book, Settlement Risk, Reputation Risk, Strategic Risk and Compliance Risk as well as various levels of stress tests. Following the guidelines issued by the Central Bank of Oman in December 2012, assessment under ICAAP is carried out and submitted to the Central Bank of Oman in accordance with the prescribed guidelines. The bank will also factor in the regulatory guidelines, wherever applicable on Basel III, while carrying out its assessment.

Quantitative Disclosures:

Position as at 31.12.2017 (RO'000)

Details	Amount
Tier I capital (after supervisory deductions)	**517,088**
Tier II capital (after supervisory deductions & upto eligible limits)	**39,230**
Tier III capital (upto a limit where Tier II & Tier III does not exceed Tier I)	-
Of which, total Eligible Tier III Capital	-
Risk Weighted Assets (RWAs) – Banking Book	**2,866,423**
Risk Weighted Assets (RWAs) – Operational Risk	**252,475**
Total Risk Weighted Assets (RWAs) – Banking Book + Operational Risk	**3,118,898**
Minimum required capital to support RWAs of banking book and operational risk	413,254
Minimum required capital comprises of;	
i) Tier I capital	376,520
ii) Tier II capital	36,734
Balance Tier I capital available for supporting Trading Book	142,814
Balance Tier II capital available for supporting Trading book	-
Risk Weighted Assets (RWAs) – Trading Book	**87,989**
Total capital required to support Trading Book	11,659
Minimum Tier I capital required for supporting Trading Book	3,323
Total Regulatory Capital	**556,318**
Total Risk Weighted Assets – Whole bank	**3,206,887**
BIS Capital Adequacy Ratio	**17.3**

Basel III Disclosures:

In compliance with CBO circular BM 1114 dated 17 November 2013; certain mandatory capital adequacy disclosures are made below:

Position as at 31.12.2017 (RO'000)

Details.	Gross balance (Book value)	Net balance (Book value)	Risk Weighted Assets
On balance sheet items	3,560,723	3,419,907	2,622,913
Off balance sheet items	259,470	259,470	243,299
Derivatives	6,511	6,511	6,511
Operational Risk	-	-	252,475
Market Risk	-	-	87,989
Total	**3,826,704**	**3,679,588**	**3,206,887**
Common equity Tier I Capital	-	-	401,588
Additional Tier 1 Capital	-	-	115,500
Tier 2 Capital	-	-	39,230
Total Regulatory Capital	-	-	**556,318**
Total required Capital @ 13.25%			424,913
Capital requirement for credit risk	-	-	379,801
Capital requirement for market risk	-	-	11,659
Capital requirement for operational risk.	-	-	33,453
Common equity Tier 1 Ratio			12.5
Tier I Ratio	-	-	16.1
Total Capital ratio	**-**	**-**	**17.3**

RISK EXPOSURE AND ASSESSMENT:

Risk Management

The primary objective of risk management is to safeguard the Bank's resources from the various risks which the Bank faces. The Risk Group comprises Corporate Credit Risk, SME Credit Risk, Retail Credit Risk, Market Risk, Operational Risk, Information Security and Business Continuity Risk and Loan Review section. All risk management functions report to Chief Risk Officer and are independent from Business Units.

The Bank's Credit Risk Strategy is aimed at adopting a structured approach to credit growth and de-emphasizing areas that are considered relatively high risk based on the prevailing and expected market conditions.

The administrative framework and the policies and procedures in place for the management of risks are based on international best practices, the recommendations of the Basel Committee and the guidelines of the Central Bank of Oman.

The Bank has exposure to the following risks:-

Credit Risk

Qualitative Disclosures:

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fail to meet its contractual obligations, and arises principally from the Bank's loans and advances to customers and other banks and investment securities. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

The Bank manages and controls credit risk by setting internal limits on the amount of risk it is willing to accept for individual counterparties and groups (single obligors) and industry sectors in line with the guidelines of Central Bank of Oman. The Bank computes expected losses on credit exposure on the basis of risk classification of both corporate and retail loans in the delinquent category based on the guidelines of Central Bank of Oman. The objective of the Bank in management of credit risk is to protect the credit quality of its credit exposures. Credit Risk is managed within the regulatory requirement of Central Bank of Oman, risk framework provided in the Risk Charter and Credit Policies and Procedures.

The policies and procedures are periodically reviewed by the Management and the Board Risk Committee to ensure alignment to the current best practices. Credit exposures are approved by delegated authorities based on delegation by the Board and Board Risk Committee. The delegation of authorities is based on the size of the single obligor exposure, the credit quality (internal, external rating) as well as level of credit risk mitigation (collateral, guarantees, etc.) for the proposed exposures. For retail exposures, there is delegation of authority for handling exceptions to approved program lending. Control, monitoring and management of credit exposures are done in coordination with respective Business Units as per established procedures.

The Bank has in place a robust credit risk management structure comprised of Corporate Credit Risk, SME credit risk, Retail Credit Risk, Loan Review Mechanism, Remedial Management and Credit Administration and Control Divisions.

Corporate credit Risk and SME Credit Risk:

Corporate Credit Risk Division is responsible for independent assessment and control of the risks related to all Corporate Banking and Financial Institutions exposures while SME Credit Risk Division independently reviews Business Banking and Small Business Unit exposures. Both the Division reviews and assesses credit risk for proposed exposures prior to facilities being committed to customers by the concerned business units. Renewals and reviews of facilities are subject to the same process. Each proposal is also assessed with respect to established concentration limits for various economic sectors, countries, risk grades, etc. and deviations, if any are highlighted. The bank follows risk based pricing and each credit proposal is also assessed based on internal benchmarks of required risk adjusted returns. The bank has implemented a customized Moody's Risk Analyst model for risk rating corporate borrowers. Corporate Credit Risk Division also provides advice and guidance to business units with a view to promoting best practices throughout the bank in the management of credit risk.

In addition to formal annual credit risk reviews of each corporate facility, more frequent reviews are also undertaken for watch list accounts, public companies and large exposures. Further, the bank continues to undertake quarterly review of financial institutions and country portfolio including stress tests and review of adverse rating migrations and outlooks in line with best practices and regulatory guidelines.

Retail Credit Risk:

Retail Credit Division manages the credit risk in the retail portfolio. Credit facilities are offered to retail customers primarily based on Product Programs. A programmed lending approach contains standard risk acceptance criteria and loan processing practices in order to optimize the efficiency and risk/ reward of those portfolios. Product programs are approved by Board Risk Committee and their performance is monitored on a regular basis and reviewed.

Based on the prevailing market conditions, the Bank sustained its continuous monitoring of the portfolio with a thorough review of the Credit Policy / Product Program. Credit facilities outside the Product Programs / Policy Parameters are individually reviewed and assessed by the Retail Banking division & the Retail Credit Risk Division.

Several system enhancements and new processes have been introduced across critical activities to improve processing quality and efficiency and to enhance the recovery methodologies of the retail portfolio. The Bank has an automated Loan Collection System in order to enhance its collections and recovery processes. It also has an automated Loan Origination System to further enhance its Retail Credit Risk framework.

Loan Review Mechanism

An independent Loan Review Mechanism Division evaluates the quality of loan book, balance between risk and reward and brings about qualitative improvements in credit administration. The division evaluates effectiveness of loan administration, integrity of credit grading process, assessment of general and specific loan loss provisions, portfolio quality, etc.

Remedial Management:

Remedial Management is responsible for pursuing each delinquent account, by using all available measures, to reduce exposure to high risk groups, to maximize recoveries, rehabilitating these relationships so that they can be returned to the business lines as fully performing accounts and progressively improve the status of the portfolio.

Credit Administration and Control:

The Credit Administration and Control section ensures:

- Documentation for all loans is properly completed, executed and maintained.
- The correct approving authority approves credit lines and details are accurately recorded.
- Production of adequate and accurate reports covering various credit risk exposures.
- Irregularities are reported and corrective action is taken.
- Review of and participation in any new/existing product offerings of the Bank.
- Various internal reporting and external reporting is prepared on a periodical basis.
- That all approved limits are input into the system under a "maker and checker" concept.
- Disbursement of funds for all approved credit exposures is appropriately authorized.

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Risk Reporting and Measurement Systems

The scope and nature of the risk reporting and/or measurement system are as follows:

Risk Reporting

A comprehensive review of the Corporate Credit Portfolio is conducted on a quarterly basis and provided to the Senior Management and the Risk Committee of the Board. Salient areas covered in the review include:

- Exposures downgraded/negatively migrated
- Weighted average credit grade profile
- Portfolio concentration/ performance
- Position of restructured exposures
- Position of past due exposures
- Exposures secured by equity
- Exposures to real estate and leasing sectors
- Syndicated exposures
- New relationships
- Exposures to senior members and non-resident borrowers
- Exposures to countries / financial institutions

In addition, the bank conducts industry studies in various sectors considered to have a bearing on the portfolio credit quality, such as, real estate, leasing, and sectors impacted by volatility in commodity prices. For FIG exposures the bank conducts stress tests and quarterly reviews of adverse rating migrations and outlooks in line with best practices and regulatory guidelines. These reports are reviewed periodically by the Management and Board Risk Committees.

A review of the Retail Credit Portfolio is conducted on a monthly basis and provided to the Management Risk Committee, and every quarter the latest report is presented to the Board Risk Committee. Salient areas covered in the review include:

- Portfolio review
- Management summary, delinquency and NPA trends (including product-wise delinquency analysis, vintage analysis, delinquencies across various credit criteria, etc.)
- Projects undertaken / fulfilled during the month
- Recoveries

Measurement:

Currently the Bank computes the expected losses on its credit exposure on the basis of risk classification of both corporate and retail loans to delinquent category based on guidelines of the Central Bank.

The Bank obtains collateral/ credit mitigants against loans and advances in the form of mortgage over property, pledges over cash/ securities, guarantees, etc. Estimates of fair value are based on the value of the collateral assessed at the time of borrowing and at regular intervals as per internally approved procedures - every three years for properties, daily for equities, etc. Collateral generally is not held against credit exposures to banks.

Definition of past due and impaired:

A loan, where repayments of principal and interest are pre-determined, shall be considered as past due, when it has not been paid on the due date fixed by the Bank, as per terms of sanction.

Credit facilities like overdrafts, lines of credit, etc. where no definite repayments are pre-determined shall be treated past due, if:

- The outstanding balance remains continuously in excess of 10% of the sanctioned/authorized limit, or
- In cases where the outstanding balance in the principal operating account is less than the sanctioned/authorized limit, but there are not enough credits in the account to cover the interest charged, or
- In cases where unauthorized drawings have frequently been allowed.
- Bills, which remain unpaid on due dates, shall be considered as past due.

All loans and advances, which are classified as substandard, doubtful and loss, are categorized as Non-Performing Loans ("NPL") i.e. impaired assets.

An evaluation is made on an ongoing basis, at least quarterly, to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the net present value of future anticipated cash flows, recognized in the income statement.

Credit Risk Management Policy:

A comprehensive set of Corporate Credit Risk Policy and Procedures Manuals, provides detailed policy guidelines and embedded

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in which are the regulatory/ in-house limits. Further, procedures manuals provide detailed process guidelines about the credit process and the templates to be used to process the individual credit applications. Financial Institutions Group (FIG) exposures are managed as per the Financial Institutions Policy guidelines. Retail Credit Policy outlines the policy guidelines related to retail banking and covers product programs and parameters relating to Salary Related Loans, Mortgages, Credit Cards and other retail product offerings. Credit Policies and Procedures are periodically reviewed to ensure that they are aligned to the market and regulatory guidelines

Quantitative Disclosure:

(i) Total gross credit exposures, plus daily average of gross exposure over the period broken down by major types of credit exposure as at 31 December 2017:

(RO'000)

S. No	Type of Credit Exposure	Average Gross Exposure		Total Gross Exposure as at	
		Current Year	Previous Year	31 December 2017	31 December 2016
1	Overdrafts	73,214	79,860	99,990	87,419
2	Personal loans	1,305,317	1,284,937	1,360,285	1,339,426
3	Loans against trust receipts	112,650	139,817	58,830	120,806
4	Other loans	1,241,257	1,201,775	1,210,774	1,148,421
5	Bills purchased / discounted	65,085	60,928	40,523	72,224
	Total	**2,797,523**	**2,767,316**	**2,770,402**	**2,768,296**

(ii) Geographic distribution of exposures by major types of credit exposure as at 31 December 2017:

(RO'000)

S. No	Type of Credit Exposure	Oman	Other GCC countries	Pakistan	Others	Total
1	Overdrafts	83,457	16,523	-	9	99,990
2	Personal loans	1,359,602	531	-	151	1,360,284
3	Loans against trust receipts	57,097	1,734	-	-	58,830
4	Other loans	1,079,528	122,357	7,744*	1,146	1,210,775
5	Bills purchased / discounted	39,230	1,293	-	-	40,523
	Total	**2,618,914**	**142,438**	**7,744***	**1,306**	**2,770,402**

*Note: The exposure is fully secured by an unconditional and irrevocable guarantee of a Government related entity based out of Oman.

(iii) Industry or counter party type distribution of exposures, broken down by major types of credit exposure as at 31 December 2017:

(RO'000)

Sr No	Economic Sector	Overdraft	Loans	Bills Purchased / Discounted	Others	Gross Total	Off Balance Sheet Exposure
1	Import Trade	-	57,079	-	-	57,079	-
2	Export Trade	-	-	-	-	-	-
3	Wholesale & Retail Trade	18,409	115,507	2,631	9,734	146,281	73,575
4	Mining & Quarrying	2,988	70,305	3,456	40	76,789	3,594
5	Construction	17,033	144,523	22,565	9,215	193,336	216,810
6	Manufacturing	10,213	146,621	5,102	29,247	191,183	42,970
7	Electricity, gas and water	509	163,526	337	1,878	166,250	1,259
8	Transport and Communication	1,130	9,192	715	575	11,612	9,017
9	Financial Institutions	11,146	175,432	-	2,266	188,844	35,237
10	Services	11,978	245,278	3,661	4,855	265,772	20,581
11	Personal Loans	9	1,360,254	-	-	1,360,263	269
12	Agriculture and Allied Activities	973	4,573	148	43	5,737	211
13	Government	-	980	-	-	980	-
14	Non-Resident Lending	-	18,207	-	-	18,207	-
15	All Others	25,602	59,582	1,908	977	88,069	43,584
	Total	**99,990**	**2,571,059**	**40,523**	**58,830**	**2,770,402**	**447,107**

(iv) Residual contractual maturity as at 31 December 2017 of the whole loan portfolio, broken down by major types of credit exposure:

(RO'000)

Sr No	Economic Sector	Overdraft	Loans	Bills Purchased / Discounted	Others	Total	Off Balance Sheet Exposure
1	Up to 1 month	4,999	184,412	15,849	26,773	232,033	90,106
2	1-3 months	4,999	91,381	18,758	18,929	134,067	148,131
3	3-6 months	4,999	123,963	5,916	1,444	136,322	61,631
4	6-9 months	4,999	53,283	-	11,684	69,966	53,916
5	9-12 months	4,999	171,569	-	-	176,568	48,477
6	1-3 years	24,998	344,161	-	-	369,159	40,593
7	3-5 years	24,998	234,773	-	-	259,771	4,204
8	Over 5 years	24,999	1,367,517	-	-	1,392,516	49
	Total	**99,990**	**2,571,059**	**40,523**	**58,830**	**2,770,402**	**447,107**

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(v) Total loan broken down by major industry or counter party type as at 31 December 2017:

(RO'000)

S. No	Economic Sector	Gross Loans	Of which, NPLs	General Provisions held	Specific Provisions held	Reserve Interest	Provisions made during the year	Advances written off during the year
1	Import Trade	57,313	-	573	-	-	-	-
2	Export Trade	-	-	-	-	-	-	-
3	Wholesale & Retail Trade	146,184	17,537	1,462	11,267	1,936	5,718	36
4	Mining & Quarrying	76,790	270	768	178	91	-	-
5	Construction	193,337	5,285	1,933	2,911	489	1,295	21
6	Manufacturing	191,183	30,290	1,912	12,883	7,898	3,601	-
7	Electricity, gas and water	166,249	-	1,662	-	-	-	-
8	Transport and Communication	11,614	3,090	116	1,797	846	306	-
9	Financial Institutions	188,844	-	1,888	-	-	1	1
10	Services	265,772	18,675	2,658	10,939	1,166	4,933	2
11	Personal Loans	1,360,226	28,030	23,005	14,570	1,759	9,258	9,290
12	Agriculture and Allied Activities	5,737	1,318	57	431	762	-	-
13	Government	980	-	10	-	-	-	-
14	Non-Resident Lending	18,207	-	182	-	-	-	-
15	All Others	87,966	8,434	615	8,965	801	-	-
	Total	**2,770,402**	**112,929**	**36,842**	**63,941**	**15,748**	**25,112**	**9,350**

(vi) Amount of impaired loans as at 31 December 2017, broken down by significant geographical areas including, with the amounts of specific and general allowances related to each geographical area:

(RO'000)

S. No	Gross Loans	Gross Loans	Of which, NPLs	General Provisions Held	Specific Provisions held	Reserve Interest	Provisions made during the year	Advances written off during the year
1	Oman	2,618,914	64,482	34,865	35,584	12,519	11,141	9,350
2	Other GCC Countries	142,438	48,296	1,887	28,245	3,192	13,971	-
3	OECD Countries	-	-	-	-	-	-	-
5	Pakistan	7,744	-	77	-	-	-	-
6	Others	1,306	151	13	112	37	-	-
	Total	**2,770,402**	**112,929**	**36,842**	**63,941**	**15,748**	**25,112**	**9,350**

(vii) Movement of gross loans

(RO'000)

Movement of Gross Loans during the year ended 31 December 2017							
Details		Performing Loans		Non-performing Loans			
Sr No	Economic Sector	Standard	Special Mention	Sub-Standard	Doubtful	Loss	Total
1	Opening balance	2,516,187	178,246	8,879	21,515	43,469	2,768,296
2	Migration / changes (+/-)	(136,189)	52,476	8,988	47,179	27,546	-
3	New loans	996,840	120	231	865	5,489	1,003,545
4	Recovery of loans	(884,865)	(65,342)	(5,559)	(31,640)	(4,683)	(992,089)
5	Loans written off	-	-	-	-	(9,350)	(9,350)
6	Closing balance	**2,491,973**	**165,500**	**12,539**	**37,919**	**62,471**	**2,770,402**
7	Provisions held	36,842	-	3,123	14,413	46,405	100,783
8	Reserve interest	-	-	192	1,334	14,222	15,748

Credit Risk –Disclosures for portfolios subject to the standardized approach.

Qualitative Disclosures:

- The bank is following Moody's rating for both sovereign and interbank exposures and the balance is treated as unrated at 100% risk.
- With the approval of the CBO, the bank uses the discretion to treat loans and advances as unrated at risk weight of 100%, except housing loans which are risk weighted at 35% based on the requirements as stipulated in the guidelines issued by CBO.
- Similarly, with the approval of CBO, the bank uses the discretion of the simple approach for recognising collaterals.

Quantitative Disclosures:

Gross exposure amount as at 31 December 2017, subject to the standardized approach is as below:

(RO'000)

S. No	Product / Rating	Carrying %0	Carrying 20%	Carrying %35	Carrying %50	Carrying %100	Carrying 150%	Total
	Rated							
1	Sovereign	476,668	-	-	-	11,496	-	488,163
2	Banks	-	66,368	-	44,659	29,814	4	140,844
	Unrated							
1	Corporate	-	4,635	-	-	1,142,484	-	1,147,119
2	Retail	-	-	-	-	929,007	-	929,007
3	Claims secured by residential property	-	-	290,605	-	112,633	-	403,238
4	Claims secured by commercial property	-	-	-	-	166,868	-	166,868
5	Past due loans	-	-	-	-	108,798	-	108,798
6	Other assets	51,378	1,606	-	-	122,989	419	176,392
7	Venture Capital & Private Equity Investments	-	-	-	-	-	295	295
8	Off-balance Sheet Items	7,634	2,408	-	13,220	242,716	3	265,979
	Total Banking Book	**535,680**	**75,016**	**290,605**	**57,879**	**2,866,804**	**720**	**3,826,704**

Credit Risk Mitigation

Qualitative Disclosures:

The bank holds collateral against loans and advances to customers in the form of cash, government development bonds, acceptable financial securities, mortgage interest over property, and other registered charge over assets, and guarantees. Estimates of fair value are based on the value of the collateral assessed on an on-going basis.

The Bank has adopted the simple approach for collaterals.

Quantitative Disclosures:

(RO'000)

Sr No	Details	Amount
1	Corporate Cash Collateral	67,425
2	Specific provisions and reserve interest on loans and advances and due from banks	79,690
	Total	**147,115**

Capital charge for credit risk under basic indicator approach as per Basel II is RO (000s) 379,801.

The Risk weighted assets for credit risk as per Basel II is RO (000s) 2,866,009

Market Risk

The objective of Bank's Market Risk Mangement is to manage and control market risk exposures which arises from fluctuations in interest rates, foreign exchange rates and equity prices while maintaining a market profile consistent with Bank's risk appetite . The board has set limits for acceptable levels of Market Risk. The Assets and Liabilities Committee (ALCO) monitors the exposure on a regular basis. Market Risk is managed based on Central Bank of Oman guidelines and the Market Risk Policy, which is approved and periodically reviewed by the Board Risk Committee. Separate Market Risk policies exist for the Bank's operations in Egypt and UAE to be compatible with the local regulatory and operational environments. Stress tests are also conducted periodically to analyze the impact of Bank and market specific stress factors crises on the earnings and capital of the Bank. The results are reviewed by ALCO, Management and Board Committees.

Market Risk Division provides risk-weightings for treasury products in line with best practices based on potential future exposure. The middle-office along with Treasury and Investment Banking Operations monitors the Market Risk positions of the Bank.

Trading Book

Foriegne Exchange Risk is the risk that the Bank may suffer losses as a result of adverse exchange rate movements.

The exposure under the trading book of the Bank includes relatively small foreign exchange exposure primarily arising from the holding of day-end positions in currencies overnight, and exposure towards interest rate related instruments. Positons are monitored on daily basis to ensure open curreny position is maintained within the regulatory limit of 40% of networth.

Value-at-risk (VaR) is used to estimate the potentioal losses on risk positions as a result of movemnets in market rates and prices. The VaR is computed every month for all non-pegged currencies in which the Bank's end-of-the-day position is above a minimum threshold. The VaR is reviewed by ALCO, Management Risk Committee and Board Risk Committee.

The Bank holds a small Held for Trading (HFT) book consisting of investments in equities which is managed by the Investment Banking division. The exposures are daily monitored by the Middle Office as per the approved stop loss and exposure limits through Mark-to-Market (MTM) reports.

For the purpose of capital charge, the three month average of the sum of the net short positions or net long positions, whichever is higher, is taken. The average is worked out on the basis of the actual positions as obtained on all the working days during the three month period immediately preceding the reporting date. The capital charge is computed at 13.25% to reflect the general market risk.

Capital Charge for trading book under Basic Indicator Approach as per Basel II is RO (000s) 11,659

The Risk weighted assets for trading risk as per Basel II is RO (000s) 87,989.

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Banking book

Equity Price Risk

The proprietary equity positions are held in the 'Available for Sale' (AFS) category as part of Banking book exposure and not in the 'Held for Trading' category. As such, no VaR is calculated for the AFS portfolio. These are marked to market on a daily basis which are circulated to the management and required actions, if any, are promptly taken as per the investment Policy, which inter-alia provides sector concentration limits, trigger levels and other guidelines for prudent management of the portfolio.

Interest Rate Risk

The principal market risk to which non-trading portfolio is exposed is the risk of loss from fluctuation in the future cash flows or fair values of financial instruments because of changes in market interest rates. Interest rate risk arises from the possibility that changes in interest rates will affect future profitability or the fair values of financial instruments. The Bank is exposed to interest rate risk as a result of mismatches of interest rate re-pricing of assets and liabilities.

Interest rate risk is managed by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard interest rate scenarios. Standard scenarios that are considered on a monthly basis include a 200 basis point (bp) parallel fall or rise in yield curves to review the impact on the economic value of the assets and liabilities and the equity of the Bank and impact on the earnings of the Bank up to one year.

In respect of monitoring the impact of interest rate changes on the earnings of the Bank, the Bank has set internal limits. Positions are monitored on a monthly basis and hedging strategies used to ensure positions are maintained within established limits.

The methods for interest rate sensitivity analysis are a traditional Maturity Gap Analysis (to measure the interest rate sensitivity of earnings), and duration (to measure interest rate sensitivity of capital) as per methodology provided by Basel Committee in 2004.

Quantitative Disclosures:

The assumptions used to measure the sensitivity is parallel shift in interest rate by 200 basis points (bps) to measure the interest sensitivity of earnings and interest rate sensitivity of capital.

As at December 2017	200 bps increase	200 bps decrease
Earnings impact - RO'000s	7,151	(7,151)
Earnings impact - USD'000s	18,575	(18,575)

The bank has been consistently using the above methods/assumptions to conduct interest rate sensitivity analysis. The analysis is carried out at monthly rests and results thereof monitored against the in-house prescribed limits; the results are also actively deliberated at the ALCO meetings. The interest rate riskof the Bank have been within the prescibed limit during the year.

The bank's interest sensitivity position, in line with guidelines issued by Central bank of Oman, based on contractual re-pricing arrangements at 31 December 2017 was as follows:

	Average effective interest rate	On demand within 3 months RO'000	3 to 12 months RO'000	1 to 5 years RO'000	Over 5 years RO'000	Non-interest sensitive RO'000	Total RO'000
Cash and balances with Central Banks	N/A	-	-	-	-	383,111	383,111
Due from banks and other money market placements (net)	2.37%	74,081	22,099	-	-	42,490	138,670
Loans, advances and financing activities for customers (net)	5.36%	859,385	600,778	664,225	529,483	-	2,653,871
Financial investments	3.45%	8,955	7,510	54,344	74,247	38,064	183,120
Premises and equipment	N/A	-	-	-	-	65,795	65,795
Other assets	N/A	-	-	-	-	45,785	45,785
Total assets		942,421	630,387	718,569	603,730	575,245	3,470,352
Due to banks and other money market deposits							
Customers' deposits and unrestricted investment accounts	4.65%	118,390	3,878	-	-	3,489	125,757
Euro medium term notes	1.64%	315,216	1,100,687	273,338	-	772,026	2,461,267
Other liabilities	3.02%	-	-	230,906	-	-	230,906
Taxation	N/A	1,782	-	-	-	71,565	73,347
Subordinated debt	N/A	-	-	-	-	7,816	7,816
Shareholders' equity	7.88%	-	-	115,500	-	-	115,500
Tier 1 Perpetual Bonds	5.09%	-	7,000	18,000	-	-	25,000
Total liabilities and shareholders' equity	N/A	-	-	-	-	430,759	430,759
Total interest rate sensitivity gap		435,388	1,111,565	637,744	-	1,285,655	3,470,352
Cumulative interest rate sensitivity gap		507,033	(481,178)	80,825	603,730	(710,410)	-

Liquidity Risk

Qualitative Disclosures:

Liquidity may be defined as a Bank's ability to ensure the availability of funds to meet all on-balance sheet and off-balance sheet commitments at a reasonable price. Liquidity Risk occurs when the Bank is unable to meet short term obligation when falling due which may raise a potentialrisk to earnings and capital of the Bank. Conversely, liquidity risk also manifests itself in the form of opportunity losses due to holding excess liquidity relative to liabilities.

The strategy of the Bank in management of liquidity risk is to minimize the resultant impact on the earnings of the Bank. The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or impacting Bank's reputation. The Bank manages the liquidity risk based on Central Bank of Oman guidelines , Liquidity Risk Policy and Liquidity Contingency Plan.

NBO takes a two-tiered approach to Liquidity Risk Management:

Going concern Liquidity Management - management of the liquidity position within specified parameters to ensure all liabilities can be met on a timely basis.

Event Risk Liquidity Management - ensuring that in the event of either a firm-specific or general market event, the Bank is able to generate sufficient liquidity to withstand a short term liquidity crisis. Event Risk Liquidity Management includes the following tools:

- Stress test: a quantitative analysis of liquidity impact of several (market and bank specific) liquidity crises.
- Liquidity buffer: mitigation of an event risk is achieved through the provision of standby liquidity in the form of unencumbered, Central Bank eligible collateral and stand-by lines.
- Contingency Funding Plan: A comprehensive Liquidity Contingency Plan that documents the procedures that the Bank would adopt to withstand either temporary or prolonged disruptions in its ability to fund some or all of its activities in a timely manner and at a reasonable cost.

The overall Liquidity Risk is kept at such a level that NBO is able to resume its business after a specified crisis.

Treasury division of the Bank receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Treasury division maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities and inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole.

The Bank is subject to liquidity limits prescribed by the CBO. Additionally, the Bank has also set internal mismatch limits by currency and limits for ensuring that liquidity lines are sufficient to meet short term maturing obligations.

The liquidity position is monitored through the Statement of Maturities of Assets and Liabilities to ensure that the gaps are within the regulatory and internal limits. The Bank also periodically conducts stress tests on liquidity based on market and bank specific scenarios .

Management periodically reviews the strategy and policies related to management of liquidity to ensure that necessary actions are implemented for monitoring and controlling liquidity risk.

The Bank has in place an effective and efficient liquidity risk management structure comprising an active ALCO which meets at monthly intervals and more frequently, if required. ALCO is kept informed regularly of the liquidity position of the Bank and immediately if there are any material changes in the Bank's current or prospective liquidity position.

The scope and nature of the risk reporting and/or measurement system:

Scope and Nature of Risk Reporting:

Maturities of Assets and Liabilities is prepared on a monthly basis and more frequently, as required, setting out the maturity profile of the various assets and liabilities and off-balance sheet items. The statement contains the cumulative gaps vis-à-vis cumulative liabilities for each prescribed time band and the position of these gaps vis-à-vis the Regulatory and in-house limits is also reported therein. This statement is placed before the ALCO at its meetings and in case any of the gap limits is exceeded, the same is escalated immediately to the ALCO along with analysis and further action planned to bring the position within the limits.

A Liquidity Lines statement is also prepared based on assumptions set out in the Liquidity Policy to evaluate the Bank's ability to meet its liabilities maturing in one month time band. Further, the liquidity of the Bank is assessed under bank specific and market specific stress scenarios and impact on gap positions and Liquidity Lines is estimated. Daily Financial Risk Report is used for monitoring the daily ratios and gaps and Early Warning Indicators for assessing any potential liquidity impact of leading indicators. These reports are regularly reviewed by the ALCO, Management and Board Risk Committee.

Measurement:

The monitoring and control of Liquidity Risk is done on an ongoing basis. The Bank uses the maturity ladder approach, which calculates the cumulative surplus or deficit of funds at selected time bands. The cash flows are placed in different time bands based on future behavior of assets, liabilities and off-balance sheet positions. In order to ensure uniformity in the treatment of behavioral patterns of assets, liabilities and off-balance sheet positions, the Central Bank has evolved a broad framework, which has been subscribed to by the Bank. In addition, the Bank regularly evaluates its liquidity position with respect to the liquidity ratios prescribed in the Liquidity Risk Policy.

The Bank has put in place "Liquidity Risk Policy" and "Liquidity Contingency Plan"- duly approved by the Board Risk Committee, which provides detailed guidelines for mitigating the risk. In case of a contingency, the policy provides a blue-print for asset sales, market access and restructuring the maturity and composition of assets and liabilities.

As an on-going mitigant the Bank has in place the availability of liquidity support in the form of committed lines of credit and reciprocal arrangements. The continuing availability of the CBO liquidity window, which was introduced in the wake of the global financial crisis, is also one of the mitigants of the liquidity risk. Besides, the Bank ensures the liquidity of certain assets as per the Liquidity Contingency Plan as a buffer against liquidity events.

The Bank has also put in place Country and Transfer Risk Policies to primarily control and monitor cross border exposures.

Basel III Liquidity Framework

The Central Bank of Oman has issued guidelines on the implementation of Basel III liquidity framreork which are Liquidity Coverage Ratio (LCR) and Net Stable Funding (NSFR) .

Liquidty Coverage Ratio (LCR)

The Liquidity coverage ratio (LCR) is a short time ratio designed to increase resilience against a liquidity shortage of up to 30 days. The LCR is computed as per CBOrequirement under the circular BM1127 (BASEL III : Framework on Liquidity coverage ratio and LCR disclosure standards). It is applicable from January 1, 2015 with a minimum ratio of 60% and increasing by 10% every year thereafter till it reaches a minimum required level of 100% on January 1, 2019, as per the time-line given below:

	1 Jan 2015	1 Jan 2016	1 Jan 2017	1 Jan 2018	1 Jan 2019
Minimum LCR	60%	70%	80%	90%	100%

Liquid Coverage Ratio as per Basel III based on weighted average value is 280.52%

Net Stable Funding Ratio (NSFR)

The standard of Net Stabe Funding Ratio (NSFR) is a longer term structural ratio designed to address liquidity mismatches and reduce funding risk over a one year horizon. It is effective Janauray 2018, with a minimum ratio of 100% as per the regulatory guidance.

Net Stable Funding Ratio (NSFR) as per Basel III is 110% as of 31 December 2017.

Quantitative Disclosures:

The maturity profile of the assets and liabilities in line with guidelines issued by Central bank of Oman, at 31 December 2017 was as follows:

	On demand within 3 months	3 to 12 months	Subtotal less than 12 months	1 to 5 years	Over 5 years	Subtotal over 12 months	Total
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Banks	323,582	25,475	349,057	17,907	16,147	34,054	383,111
Due from banks and other money market placements (net)	107,331	20,174	127,505	1,540	9,625	11,165	138,670
Loans, advances and financing activities for customers (net)	366,100	295,458	661,558	628,930	1,363,383	1,992,313	2,653,871
Financial investments	95,070	1,972	97,042	16,065	70,013	86,078	183,120
Premises and equipment	-	-	-	-	65,795	65,795	65,795
Other assets	40,372	4,554	44,926	859	-	859	45,785
Total assets	932,455	347,633	1,280,088	665,301	1,524,963	2,190,264	3,470,352
Due to banks and other money market deposits	83,379	3,878	87,257	38,500	-	38,500	125,757
Customers' deposits and unrestricted investment accounts	694,205	766,791	1,460,996	540,763	459,508	1,000,271	2,461,267
Euro medium term notes	-	-	-	230,906	-	230,906	230,906
Other liabilities	68,657	3,782	72,439	908	-	908	73,347
Taxation	7,816	-	7,816	-	-	-	7,816
Subordinated debt	-	7,000	7,000	18,000	-	18,000	25,000
Shareholders' equity	-	-	-	-	430,759	430,759	430,759
Tier 1 perpetual bonds	-	-	-	-	115,500	115,500	115,500
Total liabilities and shareholders' equity	854,057	781,451	1,635,508	829,077	1,005,767	1,834,844	3,470,352

Operational Risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Bank is able to manage the risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff training and assessment processes, including the use of internal audit.

The bank follows basic indicator approach for determining operational risk.

The Capital charge for operational risk under Basic Indicator approach is calculated by taking the average of gross income multiplied by 15%, for each of the last three financial years, excluding years of negative or zero gross income. The gross income is Net interest income (+) Non interest income (+) Provisions for unpaid interest (-) realized profit on sale of Available for Sale (AFS) investments (-) extraordinary / irregular items of income

Capital Charge for Operational Risk under Basic Indicator Approach as per Basel II is RO (000s) 33,453.

The Risk weighted assets for operational risk as per Basel II is RO (000s) 252,475.

Insurance is another tool used by the bank as an operational risk mitigant. Insurance coverage such as Bankers' Blanket Bond (BBB), Professional Indemnity, incomplete transactions, Directors and Officers liability and cyber liability insurance etc as obtained by the bank, aim at protecting the bank from high severity risks by reducing the financial impact of the same.

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In addition to the above and in order to keep control of operational incidences / losses the bank has set in place a special operational risk appetite against which incidents / losses are being monitored regularly for possible breaches and appropriate mitigants are put in place.

BASEL III – Transition Disclosure:

Further to the Guidelines on composition of capital disclosure requirements (CP1 & CP2) issued by Central Bank of Oman, the following are the mandatory disclosures for the year ended 31 December 2017.

Basel III common disclosure during the transition of regulatory adjustments (i.e. from 1 January 2013 to 1 January 2018) (RO '000)

	AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT
Common Equity Tier 1 capital: instruments and reserves	
Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	189,317
Retained earnings	143,108
Accumulated other comprehensive income (and other reserves)	73,217
Public sector capital injections grandfathered until 1 January 2018	-
Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-
Common Equity Tier 1 capital before regulatory adjustments	**405,642**
Common Equity Tier 1 capital: regulatory adjustments	
Deferred tax assets arising from temporary differences (net of related tax liability)	(1,558)
Total regulatory adjustments to Common equity Tier 1	(2,496)
Common Equity Tier 1 capital	**401,588**
Additional Tier 1 capital: instruments	**115,500**
Additional Tier 1 capital: regulatory adjustments Nil	
Tier 1 capital	**517,088**
Tier 2 capital: instruments and provisions	
Directly issued qualifying Tier 2 instruments plus related stock surplus	-
Directly issued capital instruments subject to phase out from Tier 2	3,400
Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	-
of which: instruments issued by subsidiaries subject to phase out	-
Provisions	35,830
Tier 2 capital before regulatory adjustments	**39,230**

Tier 2 capital: regulatory adjustments	
National specific regulatory adjustments	-
REGULATORY ADJUSTMENTS APPLIED TO TIER 2 IN RESPECT OF AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT.	-
OF WHICH: Cumulative fair value gains or losses on available for sale instruments	-
Total regulatory adjustments to Tier 2 capital	-
Tier 2 capital	**39,230**
Total capital	**556,318**
Total risk weighted assets	**3,206,887**
Of which: Credit risk weighted assets	2,866,423
Of which: Market risk weighted assets	87,989
Of which: Operational risk weighted assets	252,475
Capital Ratios	
Common Equity Tier 1 (as a percentage of risk weighted assets)	12.5
Tier 1 (as a percentage of risk weighted assets)	16.1
Total capital (as a percentage of risk weighted assets)	17.3
Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus G-SIB/D-SIBbuffer requirement expressed as a percentage of risk weighted assets)	-
of which: capital conservation buffer requirement	-
of which: bank specific countercyclical buffer requirement	-
of which: D-SIB/G-SIB buffer requirement	-
Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets	4.270
National minima (if different from Basel III)	
National Common Equity Tier 1 minimum ratio (if different from Basel 3 minimum)	8.250
National Tier 1 minimum ratio (if different from Basel 3 minimum)	10.250
National total capital minimum ratio (if different from Basel 3 minimum)	13.250

Disclosure template for main features of all regulatory capital instruments

Prepared under the Guidelines on composition of capital disclosure requirements RO'000s

	Balance sheet as in published financial statements 31-Dec-17
Assets	
Cash and balances with Central Bank of Oman	375,250
Certificates of deposit	7,861
Due from banks	119,899
Loans and advances to banks	18,771
Loans and advances	2,653,871
Investments in securities	183,120
Property and equipment	65,795
Deferred tax assets	1,558
Other assets	44,227
Total assets	**3,470,352**
Liabilities	
Due to banks	125,757
Customer deposits	2,461,267
Euro medium term notes	230,906
Other liabilities	81,163
Subordinated bonds	25,000
Total liabilities	**2,924,093**
Shareholders' Equity	
Paid-upshare capital	154,852
Share premium	34,465
Legal reserve	51,617
General reserve	-
Retained earnings	166,336
Other reserves	5,073
Cumulative changes in fair value of investments	(3,184)
Subordinated debt reserve	21,600
Tier 1 perpetual bond	115,500
Total shareholders' equity	**546,259**
Total liability and shareholders' funds	**3,470,352**

Prepared under the Guidelines on composition of capital disclosure requirements RO'000s

	Balance sheet as in published financial statements 31-Dec-17	Reference
Assets		
Cash and balances with Central Bank of Oman	375,250	
Certificates of deposit	7,861	
Balance with banks and money at call and short notice	119,899	
Investments in securities	183,120	
Loans and advances Of which :		
Loans to Banks - Gross	18,865	
General Provisions considered for Tier 2	(94)	
Net Loans to banks	18,771	
Loans to Customers - Gross	2,653,871	A1
Specific Provisions	35,830	
General Provisions considered for Tier 2	(35,830)	
Net Loans to customers	2,653,871	
Fixed assets	65,795	
Other assets of which:	44,227	
Deferred tax assets	1,558	**A2**
Amount considered for CET1	-	
Current year allocation - not eligible	1,558	
Total Assets	**3,470,352**	
Capital & Liabilities		
Paid-upCapital	189,317	C1
Of which:		
Amount eligible for CET1	189,317	
Amount eligible for AT1	-	
Reverses and Surplus	166,366	C2
Of which: Amount eligible for CET1		
Retained earnings carried forward	166,366	
Profit for current year not eligible	-	
Legal reserve	51,617	C4
General reserve	-	
Subordinated debt reserve	21,600	
Proposed Stock Dividend	7,743	**C3**
Total Amount eligible for CET1	**80,960**	
Tier 1 perpetual bond	115,500	**C7**
Proposed Cash Dividend	23,228	
Cumulative changes in fair value of investments	(3,184)	

Prepared under the Guidelines on composition of capital disclosure requirements (Continued) RO'000s

	Balance sheet as in published financial statements 31-Dec-17	Reference
Amount eligible for Tier 2	-	C5
Revaluation and other reserves	5,073	
Total Capital	546,259	C6
DepositsOf which:		
Deposits from banks	125,757	
Customer deposits	2,461,267	
Deposits of Islamic Banking window	-	
Euro medium term notes	230,906	
Other deposits (Sub-debt)	25,000	
Other liabilities & provisionsOf which:	81,163	
TOTAL	**3,470,352**	

Prepared under the Guidelines on composition of capital disclosure requirements (RO '000)

Prepared under the Guidelines on composition of capital disclosure requirements	Component of regulatory capital reported by bank	Source based on reference numbers/letters of the balance sheet under the regulatory scope of consolidation from step 2
Common Equity Tier 1 capital: instruments and reserves		
Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	189,317	C1
Retained earnings	142,858	C2
Accumulated other comprehensive income (and other reserves)	73,217	C3
Public sector capital injections grandfathered until 1 January 2018	-	
Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-	
Common Equity Tier 1 capital before regulatory adjustments	405,392	
Common Equity Tier 1 capital: regulatory adjustments		
Deferred tax assets arising from temporary differences (net of related tax liability)	(1,558)	A2
Cumulative fair value gains or losses on available for sale	(2,496)	
Total regulatory adjustments to Common equity Tier 1	(4,054)	
Common Equity Tier 1 capital (CET1)	401,588	
Additional Tier 1 capital: instruments (TIER1 PERPETUAL BOND)	115,500	C7
Additional Tier 1 capital: regulatory adjustments - Nil		
Tier 1 capital (T1 = CET1 + AT1)	517,088	
Tier 2 capital: instruments and provisions		
Directly issued capital instruments subject to phase out from Tier 2	3,400	C6-C4
Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	-	
of which: instruments issued by subsidiaries subject to phase out	-	
General provisions	35,830	A1
Cumulative fair value gains or losses on available for sale instruments	-	C5
Tier 2 capital before regulatory adjustments	39,230	
Tier 2 capital: regulatory adjustments		
National specific regulatory adjustments	-	
REGULATORY ADJUSTMENTS APPLIED TO TIER 2 IN RESPECT OF AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT.	-	
OF WHICH: Cumulative fair value gains or losses on available for sale instruments	-	
Total regulatory adjustments to Tier 2 capital	-	
Tier 2 capital (T2)	39,230	
Total capital (TC = T1 + T2)	556,318	

Prepared under the Guidelines on composition of capital disclosure requirements

1. Common Equity.

Common equity comprises of 1,548,520,338 equity shares of RO 0.100 each fully paid up, issued and governed under the laws of Sultanate of Oman.

2. All other regulatory capital instruments

1	Issuer	-	National Bank of Oman	National Bank of Oman
2	Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement)	-	XS1321921899	Private Placements comprises of 8 issues
3	Governing law(s) of the instrument	-	English	Sultanate of Oman
4	Transitional Basel III rules	-	Additional Tier 1	Tier 2
5	Post-transitional Basel III rules	-	Eligible	Ineligible
6	Eligible at solo/group/group & solo	-	Solo	Solo
7	Instrument type	-	Additional Tier 1	Subordinated debts
8	Amount recognised in regulatory capital	-	RO 115.5 million	RO 3.4 million (Aggregate of 8 issues)
9	Par value of instrument	-	RO 115.5 million	RO 25.0 million (Aggregate of 8 issues)
10	Accounting classification	-	Equity	Liability –amortised cost
11	Original date of issuance	-	18-Nov-15	Between Dec 2012 to Mar 2013
12	Perpetual or dated	-	Perpetual	Dated
13	Original maturity date	-	Not applicable	Dec 2018 to Mar 2019
14	Issuer call subject to prior supervisory approval	-	Yes	Yes – 0 issue, No – 8 issues
15	Optional call date, contingent call dates and redemption amount	-	18-Nov-20	Not applicable
16	Subsequent call dates, if applicable	-	Every five years	Not applicable
Coupons / dividends				
17	Fixed or floating dividend/coupon	-	Fixed	Fixed
18	Coupon rate and any related index	-	7.875%	4.50% to 5.50%
19	Existence of a dividend stopper	-	Yes	No
20	Fully discretionary, partially discretionary or mandatory	-	Fully discretionary	Mandatory
21	Existence of step up or other incentive to redeem	-	No	No
22	Noncumulative or cumulative	-	Non cumulative	Not applicable
23	Convertible or non-convertible	-	Non convertible	Non-convertible
24	If convertible, conversion trigger (s)	-	Not applicable	Not applicable
25	If convertible, fully or partially	-	Not applicable	Not applicable
26	If convertible, conversion rate	-	Not applicable	Not applicable
27	If convertible, mandatory or optional conversion	-	Not applicable	Not applicable
28	If convertible, specify instrument type convertible into	-	Not applicable	Not applicable
29	If convertible, specify issuer of instrument it converts into	-	Not applicable	Not applicable
30	Write-down feature	-	Yes	No
31	If write-down, write-down trigger(s)	-	Non viability event	No
32	If write-down, full or partial	-	Full (See note)	No
33	If write-down, permanent or temporary	-	Permanent	No
34	If temporary write-down, description of write-up mechanism	-	Not applicable	No
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	-	Subordinated to Senior Liabilities and Tier 2 - Subordinted debts	Subordinated to Senior Liabilities
36	Non-compliant transitioned features	-	No	No
37	If yes, specify non-compliant features	-	Not applicable	Not applicable

Note: The Capital Securities can be cancelled (in the case of a write-down in whole) or written-down in part on a pro rata basis (in the case of a write-down in part) as determined by the Bank in conjunction with the Regulator in accordance with the Capital Regulations.

This report on Basel II & III disclosures was authorized for issue by the Board of Directors on 28 January 2018.

Rawan bint Ahmed Al Said

Chairperson

Statement of Financial Position as at 31 December 2017

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C.R. No. 1224013
PR No. HMH/15/2015; HMA/9/2015

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF OMAN SAOG

Report on the audit of the financial statements

Opinion

We have audited the financial statements of National Bank of Oman SAOG (the "bank"), which comprise the statement of financial position as at 31 December 2017, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the bank as at 31 December 2017 and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report. We are independent of the bank in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in the Sultanate of Oman, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of matter

We draw attention to note 22.1 of the financial statements which describes the status of the guarantees amounting to RO 14.3 million invoked by a beneficiary and legal action initiated by the bank to recover the related amount from its customer.

Our opinion is not modified in respect of this matter.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial statements.

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF OMAN SAOG (CONTINUED)

1. Impairment of loans, advances and financing activities for customers

Key audit matters	*How our audit addressed the key audit matters*
Impairment of loans, advances and financing activities to customers (loans and receivables) is a highly subjective area due to the level of judgement applied by management in determining the extent of credit losses related to such loans and receivables. The judgements applied by the management in determining the level of impairment for loans and receivables include the identification of events that could possibly result in an impairment, an appropriate valuation of the related collateral, the assessment of customers that are likely to default, and the future cash flows relating to loans and receivables. Due to the material nature of loans and receivables and the related estimation uncertainties involved, including the consideration of industry and prudential requirements, this is considered a key audit matter. The basis of the bank's impairment provision policy is presented in the accounting policies section and in Note 3.19 to the financial statements. Attention is also drawn to the critical accounting estimates and judgements, disclosures of loans and receivables and the credit risk management set out in notes 2.4.2, 6 and 30.1, respectively to the financial statements.	Our audit procedures included the assessment of controls over the granting, booking and monitoring processes of loans and receivables, and the specific and collective impairment provisioning process, including consideration of prudential requirements, to validate the operating effectiveness of the key controls in place, which identify the impaired loans and receivables and the required provisions against them. As part of the control testing procedures, we assessed whether the key controls in the above processes were designed, implemented and operated effectively. In addition to testing the key controls, we selected samples of loans and receivables outstanding as at the reporting date and critically assessed the criteria for determining whether an impairment event had occurred that would require an impairment provision. For the samples selected, we also verified whether all impairment events as identified by us had also been identified by the bank's management. Our selected samples also included non-performing loans and receivables where we assessed management's forecast of recoverable cash flows, the valuation of collaterals, estimates of recovery on default and other sources of repayment. For the performing loans and receivables, we assessed whether the borrowers exhibited any possible default risk that may affect meeting their scheduled repayment obligations. For collective impairment provisions, we obtained an understanding of the methodology used by the bank to determine the collective provisions, assessed the underlying assumptions and sufficiency of the data used by management. We also assessed whether the financial statement disclosures appropriately reflect the requirements of IFRS.

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Other information included in the bank's 2017 Annual Report

Those charged with governance and management are responsible for the other information. Other information consists of the information included in the bank's 2017 Annual Report other than the financial statements and our auditor's report thereon. We obtained the following information prior to the date of our auditor's report, and we expect to obtain the published 2017 Annual Report after the date of our auditor's report:

- Chairman's report
- Corporate governance report
- Management discussion and analysis
- Financial statements of the Islamic Banking Window
- Basel II Pillar III and Basel III Report of the bank
- Basel II Pillar III and Basel III Report of the Islamic Banking Services.

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information obtained prior to the date of the auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the financial statements

Those charged with governance are responsible for the preparation and fair presentation of the financial statements in accordance with IFRS and the relevant requirements of the Commercial Companies Law of 1974, as amended, and the Capital Market Authority ("the CMA") of the Sultanate of Oman, and for such internal control as those charged with governance determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, those charged with governance are responsible for assessing the bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless those charged with governance either intends to liquidate the bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the bank's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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Auditor's responsibilities for the audit of the financial statements (continued)

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for expressing an opinion on the effectiveness of the bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of those charged with governance's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

In our opinion, the financial statements comply, in all material respects, with the relevant requirements of the Commercial Companies Law of 1974, as amended, and CMA of the Sultanate of Oman.

Ernst & Young LLC
Sanjay

Sanjay Kawatra
Muscat
10 March 2018

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STATEMENT OF FINANCIAL POSITION

As at 31 December 2017

2016 USD'000	**2017 USD'000**		Notes	**2017 RO'000**	2016 RO'000
		Assets			
1,328,816	**995,094**	Cash and balances with Central Banks	4	**383,111**	511,594
299,558	**360,182**	Due from banks and other money market placements (net)	5	**138,670**	115,330
6,935,795	**6,893,171**	Loans, advances and financing activities for customers (net)	6	**2,653,871**	2,670,281
333,462	**475,636**	Financial investments	7	**183,120**	128,383
120,377	**170,896**	Premises and equipment	8	**65,795**	46,345
157,792	**118,922**	Other assets	9	**45,785**	60,750
9,175,800	**9,013,901**	**TOTAL ASSETS**		**3,470,352**	3,532,683
		LIABILITIES AND EQUITY			
		LIABILITIES			
585,026	**326,642**	Due to banks and other money market deposits	10	**125,757**	225,235
6,232,107	**6,392,901**	Customers' deposits and unrestricted investment accounts	11	**2,461,267**	2,399,361
605,468	**599,756**	Euro medium term notes	12	**230,906**	233,105
207,953	**190,512**	Other liabilities	13	**73,347**	80,062
19,236	**20,301**	Taxation	14	**7,816**	7,406
127,532	**64,935**	Subordinated debt	15	**25,000**	49,100
7,777,322	**7,595,047**	**TOTAL LIABILITIES**		**2,924,093**	2,994,269
		EQUITY			
383,060	**402,213**	Share capital	16	**154,852**	147,478
89,519	**89,519**	Share premium	17	**34,465**	34,465
127,686	**134,070**	Legal reserve	18	**51,617**	49,159
119,990	**61,010**	Other non-distributable reserves	19	**23,489**	46,196
60,982	**60,332**	Proposed cash dividend	21	**23,228**	23,478
19,153	**20,112**	Proposed stock dividend	21	**7,743**	7,374
298,088	**351,598**	Retained earnings		**135,365**	114,764
1,098,478	**1,118,854**	**TOTAL SHAREHOLDERS' EQUITY ATTRIBUTABLE TO THE EQUITY HOLDERS OF THE BANK**		**430,759**	422,914
300,000	**300,000**	Tier 1 Perpetual Bond	20	**115,500**	115,500
1,398,478	**1,418,854**	**TOTAL EQUITY**		**546,259**	538,414
9,175,800	**9,013,901**	**TOTAL LIABILITIES AND EQUITY**		**3,470,352**	3,532,683

The financial statements were authorised for issue on 28 January 2018 in accordance with a resolution of the Board of Directors.

Chairperson

Chief Executive Officer

The attached notes 1 to 35 form part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2017

2016 USD'000	**2017 USD'000**		Notes	**2017 RO'000**	2016 RO'000
354,434	**376,068**	Interest income	23	**144,786**	136,457
(99,613)	**(141,288)**	Interest expense	24	**(54,396)**	(38,351)
254,821	**234,780**	**Net interest income**		**90,390**	98,106
12,974	**14,548**	Income from Islamic financing and investment activities		**5,601**	4,995
(3,990)	(7,951)	Unrestricted investment account holders' share of profit		(3,061)	(1,536)
8,984	**6,597**	**Net Income from Islamic financing and investment activities**		**2,540**	3,459
263,805	241,377	Net interest income and net income from Islamic financing and Investment activities		92,930	101,565
89,735	**101,816**	**Other operating income**	25	**39,199**	34,548
353,540	**343,193**	**Operating income**		**132,129**	136,113
(98,395)	**(98,125)**	Staff costs		**(37,778)**	(37,882)
(56,930)	**(58,514)**	Other operating expenses	26	**(22,528)**	(21,918)
(7,439)	**(10,940)**	Depreciation	8	**(4,212)**	(2,864)
(162,764)	**(167,579)**	**Total operating expenses**		**(64,518)**	(62,664)
190,776	**175,614**	**PROFIT FROM OPERATIONS BEFORE IMPAIRMENT LOSSES AND TAX**		**67,611**	73,449
(51,029)	**(65,229)**	Credit loss expense – customers' loan	6	**(25,113)**	(19,646)
6,673	**7,810**	Recoveries and releases from provision for credit losses	6	**3,007**	2,569
18,678	**16,805**	Recoveries from loans and advances written off		**6,470**	7,191
(545)	**(1,787)**	Impairment losses on available-for-sale investments	7	**(688)**	(210)
161	**(68)**	Credit loss (expense) / write back - bank loans		**(26)**	62
(26,062)	**(42,469)**	**TOTAL IMPAIRMENT LOSSES (NET)**		**(16,350)**	(10,034)
164,714	**133,145**	**PROFIT BEFORE TAX**		**51,261**	63,415
(19,834)	**(18,792)**	Taxation	14	**(7,235)**	(7,636)
144,880	**114,353**	**PROFIT FOR THE YEAR**		**44,026**	55,779
		OTHER COMPREHENSIVE EXPENSE			
		Items that are or may be reclassified subsequently to profit or loss			
(3,540)	**(11,473)**	Net movement on available-for-sale investments		**(4,417)**	(1,363)
545	**1,787**	Impairment losses on available-for-sale investments already recognised in comprehensive income	7	**688**	210
(174)	**317**	Tax effect of net movement on available-for-sale investments		**122**	(67)
(3,169)	**(9,369)**	**OTHER COMPREHENSIVE EXPENSE FOR THE YEAR**		**(3,607)**	(1,220)
141,711	**104,984**	**TOTAL COMPREHENSIVE INCOME FOR THE YEAR**		**40,419**	54,559
0.08	**0.06**	Earnings per share: (USD) – Basic and diluted – (RO)	28	**0.023**	0.031

The attached notes 1 to 35 form part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2017

	Attributable to equity holders of Bank									
	Share capital	Share premium	Legal reserve	Other non-distributable reserves (note 19)	Proposed cash dividend (note 21)	Proposed stock dividend (note 21)	Retained earnings	Total	Tier 1 perpetual bond	Total
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Balance at 1 January 2017	**147,478**	**34,465**	**49,159**	**46,196**	**23,478**	**7,374**	**114,764**	**422,914**	**115,500**	**538,414**
Total comprehensive income for the year	-	-	-	**(3,607)**	-	-	**44,026**	**40,419**	-	**40,419**
Issue of bonus shares (note 21)	**7,374**	-	-	-	-	**(7,374)**	-	-	-	-
Dividend paid (note 21)	-	-	-	-	**(23,478)**	-	-	**(23,478)**	-	**(23,478)**
Interest on tier 1 perpetual bond	-	-	-	-	-	-	**(9,096)**	**(9,096)**	-	**(9,096)**
Transfer to retained earnings	-	-	-	**(24,100)**	-	-	**24,100**	-	-	-
Transfer to subordinated debts reserve (note 15)	-	-	-	**5,000**	-	-	**(5,000)**	-	-	-
Transfer to legal reserve (note 18)	-	-	**2,458**	-	-	-	**(2,458)**	-	-	-
Proposed dividend	-	-	-	-	**23,228**	**7,743**	**(30,971)**	-	-	-
Balance at 31 December 2017	**154,852**	**34,465**	**51,617**	**23,489**	**23,228**	**7,743**	**135,365**	**430,759**	**115,500**	**546,259**
Balance at 31 December 2017 – In USD'000	**402,213**	**89,519**	**134,070**	**61,010**	**60,332**	**20,112**	**351,597**	**1,118,854**	**300,000**	**1,418,854**
Balance at 1 January 2016	134,071	34,465	47,737	40,596	22,792	13,407	106,089	399,157	115,500	514,657
Total comprehensive income for the year	-	-	-	(1,220)	-	-	55,779	54,559	-	54,559
Dividend paid (note 21)	-	-	-	-	(22,792)	-	-	(22,792)	-	(22,792)
Issue of bonus shares (note 21)	13,407	-	-	-	-	(13,407)	-	-	-	-
Interest on tier 1 perpetual bond	-	-	-	-	-	-	(8,010)	(8,010)	-	(8,010)
Proposed dividend	-	-	-	-	23,478	7,374	(30,852)	-	-	-
Transfer to retained earnings	-	-	-	(3,000)	-	-	3,000	-	-	-
Transfer to subordinated debt reserve (note 15)	-	-	-	9,820	-	-	(9,820)	-	-	-
Transfer to legal reserve (note 18)	-	-	1,422	-	-	-	(1,422)	-	-	-
Balance at 31 December 2016	147,478	34,465	49,159	46,196	23,478	7,374	114,764	422,914	115,500	538,414
Balance at 31 December 2016 – In USD'000	383,060	89,519	127,686	119,990	60,982	19,153	298,088	1,098,478	300,000	1,398,478

The attached notes 1 to 35 form part of these financial statements.

STATEMENT OF CASH FLOW

For the year ended 31 December 2017

2016 USD'000	**2017 USD'000**		Notes	**2017 RO'000**	2016 RO'000
		OPERATING ACTIVITIES			
164,714	**133,145**	Profit before taxation		**51,261**	63,415
		Adjustments for:			
7,439	**10,940**	Depreciation	8	**4,212**	2,864
51,029	**65,229**	Provision for credit losses – customers' loans		**25,113**	19,646
(161)	**68**	Provision for credit losses/write back - due from banks		**26**	(62)
545	**1,787**	Impairment losses on available for sale investments	7	**688**	210
(31)	**(3)**	Profit on sale of equipment (net)		**(1)**	(12)
(4,447)	**(4,829)**	Profit on sale of investments	25	**(1,859)**	(1,712)
(11,514)	**(17,298)**	Investment income		**(6,660)**	(4,433)
207,574	**189,039**	Operating profit before changes in operating assets and Liabilities		**72,780**	79,916
(38,062)	**29,104**	Due from banks and other money market placements		**11,205**	(14,654)
225,062	**(263,694)**	Due to banks and other money market deposits		**(101,522)**	86,649
(404,748)	**(22,605)**	Loans, advances and financing activities for customers (net)		**(8,703)**	(155,828)
5,153	**40,766**	Other assets		**15,695**	1,984
388,403	**160,795**	Customers' deposits		**61,906**	149,535
100,000	**-**	Euro medium term notes		**-**	38,500
(3,268)	**(23,156)**	Other liabilities		**(8,915)**	(1,258)
480,114	**110,249**	**Cash from operations**		**42,446**	184,844
(22,358)	**(19,319)**	Taxes paid		**(7,438)**	(8,608)
457,756	**90,930**	**Net cash from operating activities**		**35,008**	176,236
		INVESTING ACTIVITIES			
(37,691)	**(246,810)**	Purchase of available-for-sale investments		**(95,022)**	(14,511)
34,527	**40,940**	Proceeds from sale of available-for-sale investments		**15,762**	13,293
77,922	**57,143**	Proceeds from maturity of government development bonds		**22,000**	30,000
(38,369)	**(61,506)**	Purchase of premises and equipment	8	**(23,680)**	(14,772)
255	**55**	Disposal of premises and equipment		**21**	98
9,545	**13,810**	Income from bond and other investments	25	**5,317**	3,675
1,969	**3,488**	Dividend income	25	**1,343**	758
(945)	**(13)**	Translation differences on premises and equipment and tax		**(5)**	(363)
47,213	**(192,893)**	**Net cash (used in)/from investing activities**		**(74,264)**	18,178

STATEMENT OF CASH FLOW

For the year ended 31 December 2017

2016 USD'000	2017 USD'000		Notes	2017 RO'000	2016 RO'000
		FINANCING ACTIVITIES			
(59,200)	**(60,982)**	Payment of dividend		**(23,478)**	(22,792)
(7,791)	**(62,597)**	Net movement in subordinated debt	15	**(24,100)**	(3,000)
-	**-**	Proceeds from Tier 1 perpetual bond		**-**	-
(20,805)	**(23,626)**	Interest on Tier 1 perpetual bond		**(9,096)**	(8,010)
(87,796)	**(147,205)**	Net cash used in financing activities		**(56,674)**	(33,802)
417,173	**(249,168)**	(DECREASE)/INCREASE IN CASH AND CASH EQUIVALENTS		**(95,930)**	160,612
888,004	**1,305,177**	Cash and cash equivalents at the beginning of the year		**502,493**	341,881
1,305,177	**1,056,009**	CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR		**406,563**	502,493
		REPRESENTING:			
1,327,517	**993,795**	Cash and balances with Central Banks	4	**382,611**	511,094
188,920	**278,782**	Due from banks maturing within three months		**107,331**	72,734
(211,260)	**(216,568)**	Due to banks maturing within three months		**(83,379)**	(81,335)
1,305,177	**1,056,009**			**406,563**	502,493

The attached notes 1 to 35 form part of these financial statements.

1. LEGAL STATUS AND PRINCIPAL ACTIVITIES

National Bank of Oman SAOG ("NBO", "the bank") was established in the Sultanate of Oman in 1973 as a joint stock company and is engaged in retail, wholesale, investment and Islamic banking services within the Sultanate of Oman and overseas branches in the United Arab Emirates and Egypt. In Oman the bank operates under banking license issued by the Central Bank of Oman and is covered by its deposit insurance scheme, whereas in the United Arab Emirates and in Egypt the branches operate under a commercial bank licences given by the respective Central Banks. The registered address of the bank is PO Box 751, Ruwi, Postal Code 112, Muscat, Sultanate of Oman. The bank has a primary listing on the Muscat Stock Exchange.

The bank employed 1,501 employees as of 31 December 2017 (31 December 2016 – 1,544 employees).

2. BASIS OF PREPARATION

2.1 Basis of measurement

The financial statements are prepared under the historical cost convention as modified to include the revaluation of freehold land and buildings and the measurement at fair value of derivatives, investments classified as available-for-sale and investments carried at fair value through profit and loss.

2.2 Functional and presentation currency

These financial statements are presented in Rial Omani rounded to the nearest thousand Rial Omani, except when otherwise indicated. The functional currencies of the bank's operations are as follows:

- Sultanate of Oman: Rial Omani
- United Arab Emirates: UAE Dirham
- Egypt: US Dollar

The United States Dollar amounts shown in the financial statements have been translated from Rial Omani at an exchange rate of RO 0.385 to each US Dollar, and are shown for the convenience of the reader only.

2.3 Statement of compliance

The financial statements of the bank have been prepared in accordance with International Financial Reporting Standards (IFRS), applicable regulations of the Central Bank of Oman and applicable requirements of the Commercial Companies Law of Oman, as amended and the Capital Market Authority of the Sultanate of Oman.

The bank also prepares a separate set of financial statements for its Islamic Banking Window (IBW) in accordance with the requirements of Section 1.2 of Title 3 of the Islamic Banking Regulatory Framework ("IBRF") issued by CBO. The separate set of financial statements of its IBW are prepared in accordance with Financial Accounting Standards ("FAS") issued by Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"), the Sharia Rules and Principles as determined by the Sharia Supervisory Board of the Islamic Window (the "SSB") and other applicable requirements of CBO. The IBWs financial statements are then converted into International Financial Reporting Standards (IFRS) compliant financial statements and included in these financial statements. All inter branch balances and transactions have been eliminated.

The bank presents its statement of financial position broadly in order of liquidity.

2.4 Significant accounting judgments and estimates

In the process of applying the bank's accounting policies, management has used its judgments and made estimates in determining the amounts recognised in the financial statements. The most significant use of judgments and estimates are as follows:

2.4.1 Going concern

The bank's management has made an assessment of the bank's ability to continue as a going concern and is satisfied that the bank has the resources to continue in business for the foreseeable future. Furthermore, the management is not aware of any material uncertainties that may cast significant doubt upon the bank's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on a going concern basis.

2. BASIS OF PREPARATION (Continued)

2.4.2 Impairment losses on loans and advances

The bank reviews its individually significant loans and advances at each reporting date to assess whether an impairment loss should be recorded in the statement of comprehensive income. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. In estimating these cash flows, the bank makes judgments about the borrower's financial situation and the net realisable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

Loans and advances that have been assessed individually and found not to be impaired and all individually insignificant loans and advances are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident. The collective assessment takes account of data from the loan portfolio (such as credit quality, levels of arrears, credit utilisation, loan to collateral ratios etc.) and concentrations of risks.

2.4.3 Impairment of equity investments

The bank treats available-for-sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires judgment.

2.4.4 Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of valuation models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgment is required to establish fair values.

2.4.5 Deferred tax assets

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

2.4.6 Investment Funds

The bank acts as fund manager and investment advisor to investment funds. For all funds managed by the bank, the investors (whose number ranges from 30 to 100) are able to vote by simple majority to remove the bank as fund manager without cause, and the bank's aggregate economic interest is in each case less than 5%. As a result, the bank has concluded that it acts as agent for the investors in all cases, and therefore has not consolidated these funds.

2.5 Standards, amendments and interpretations effective in 2017 and relevant for the bank's operations

For the year ended 31 December 2017, the bank has adopted all of the following new and revised standards and interpretations issued by the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) of the IASB that are relevant to its operations and effective for periods beginning on 1 January 2017.

- Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative
- Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses
- Annual Improvements Cycle - 2014-2016
- Amendments to IFRS 12 Disclosure of Interests in Other Entities: Clarification of the scope of disclosure requirements in IFRS 12

The adoption of these standards and interpretations has not resulted in any significant changes to the bank's accounting policies and has not affected the amounts reported for the current and prior years.

Notes to the Financial Statements
For the year ended 31 December 2017

2. BASIS OF PREPARATION (Continued)

2.6 Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the bank

IFRS 9 will have a significant impact on the bank's financial statements and details are set out below:

IFRS 9 Financial Instruments

The bank will adopt IFRS 9 on 1 January 2018 and will not restate the comparative information in accordance with relevant requirements of IFRS 9. IFRS 9 will replace IAS 39 Financial Instruments: Recognition and Measurement and introduces new requirements for the classification and measurement of financial assets and financial liabilities, a new model based on expected credit losses for recognising loan loss provisions and provides for simplified hedge accounting by aligning hedge accounting more closely with an entity's risk management methodology.

The bank has assessed the estimated impact that the initial application of IFRS 9 will have on its financial statements as below:

The bank's initial estimate of IFRS 9 is expected to impact equity attributable to the equity holders of the bank by 4 - 5% as of 1 January 2018. This is preliminary, because not all transition work has been finalised. The actual impact of adopting IFRS 9 on 1 January 2018 may change accordingly.

(i) Classification and measurement

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which financial assets are managed and the underlying cash flow characteristics. IFRS 9 contains three principal classification categories for financial assets: (a) measured at Amortised Cost (AC), Fair Value through Other Comprehensive Income (FVOCI) and Fair Value through Profit or Loss (FVPL). Under IFRS 9, derivatives embedded in contracts where the host is a financial asset are never bifurcated. Instead, the hybrid financial instrument as a whole is assessed for classification.

At 31 December 2017, the Bank had equity investments classified as available-for-sale with a fair value of RO 35.6 million that are held for long-term strategic purposes. Under IFRS 9, the Bank has designated these investments as measured at FVOCI. Due to this reclassification, an increase of RO 2.89 million is estimated in the retained earnings along with a corresponding increase in negative fair value reserve due to reclassification of impairment on equity investments measured at fair value through other comprehensive income to the reserves.

(ii) Expected credit losses

IFRS 9 replaces the 'incurred loss' model in IAS 39 with a forward-looking 'expected credit loss' (ECL) model. The new impairment model will apply to financial assets measured at amortised cost or FVOCI, except for investments in equity instruments. A number of significant judgements are also required in applying the accounting requirements for measuring ECL, such as:

- Determining criteria for significant increase in credit risk (SICR);
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL; and
- Establishing groups of similar financial assets for the purposes of measuring ECL.

The CBO has issued guidelines relating to implementation of IFRS 9. The relevant requirements relating to transition are set out below:

- Should the existing loan loss impairment computed in accordance with the requirements of IAS 39 and CBO guidelines be higher than the impairment allowance computed under IFRS 9, the related difference (net of tax) be transferred to a loan loss impairment reserve from retained earnings as of 1 January 2018.
- In the subsequent years, where the allowance for loan loss impairment computed in accordance with CBO requirements is higher than the allowance for loan loss impairment loss computed under IFRS 9, the difference (net of tax) should be transferred to the aforementioned loan loss impairment reserve from retained earnings.
- The related impairment reserve will not be available for dividend distribution or for inclusion in the regulatory capital. Any subsequent utilisation of the impairment reserve would require prior approval of the CBO.

2. BASIS OF PREPARATION (Continued)

IFRS 9 Financial Instruments (Continued)

(iii) Financial liabilities

Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.

(iv) Hedge accounting

Hedge accounting requirements of IFRS 9 are designed to align the accounting more closely to the risk management framework; permit a greater variety of hedging instruments; and remove or simplify some of the rule-based requirements in IAS 39. The elements of hedge accounting: fair value, cash flow and net investment hedges are retained.

As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, the bank does not expect a significant impact as a result of applying IFRS 9.

(v) Disclosure

IFRS 9 also introduces expanded disclosure requirements and changes in presentation. These are expected to change the nature and extent of the bank's disclosures about its financial instruments particularly in the year of the adoption of IFRS 9.

Other relevant standards which are expected to have implications on the bank's are IFRS 15 and IFRS 16 and details are set out below:

IFRS 15 - Revenue from Contracts with Customers: IFRS 15 was issued in May 2014, and amended in April 2016, and establishes a five-step model to account for revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The new revenue standard will supersede all current revenue recognition requirements under IFRS. Either a full retrospective application or a modified retrospective application is required for annual periods beginning on or after 1 January 2018. Early adoption is permitted. The bank plans to adopt the new standard on the required effective date using the modified retrospective approach. The bank has performed an initial impact assessment and concluded that the impact is not material as in majority of the bank's facility agreements with customers generally expected to be the only performance obligation and accordingly, adoption of IFRS 15 is not expected to have any impact on the bank's income and profit or loss.

IFRS 16 – Leases: The IASB issued IFRS 16 Leases (IFRS 16), which requires lessees to recognise assets and liabilities for most leases. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). For lessors, there is little change to the existing accounting in IAS 17 Leases. The bank will perform a detailed assessment in the future to determine the extent. The new standard will be effective for annual periods beginning on or after 1 January 2019. IFRS 16 also requires lessees and lessors to make more extensive disclosures than under IAS 17. In 2018, the bank will continue to assess the potential effect of IFRS 16 on its financial statements.

3. SIGNIFICANT ACCOUNTING POLICIES

3.1 Date of recognition

All financial assets and liabilities are initially recognised on the trade date, i.e., the date that the bank becomes a party to the contractual provisions of the instrument. This includes "regular way trades": purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

3.2 Initial measurement of financial instruments

The classification of financial instruments at initial recognition depends on the purpose and the management's intention for which the financial instruments were acquired and their characteristics. All financial instruments are measured initially at their fair value plus transaction costs, except in the case of financial assets and financial liabilities recorded at fair value through profit or loss where transaction costs is recorded as an expense.

3.3 Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances with banks and other financial institutions, treasury bills and money market placements, deposits and certificates of deposit maturing within three months of the date of acquisition. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.4 Financial assets and financial liabilities designated at fair value through profit or loss

Financial assets and financial liabilities classified in this category are designated by management on initial recognition when the following criteria are met:

- the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognising gains or losses on them on a different basis; or
- the assets and liabilities are part of a group of financial assets, financial liabilities or both which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or
- The financial instrument contains an embedded derivative, unless the embedded derivative does not significantly modify the cash flows or it is clear, with little or no analysis, that it would not be separately recorded.

Financial assets and financial liabilities at fair value through profit or loss are recorded in the statement of financial position at fair value. Changes in fair value are recorded in 'other operating income'. Interest is earned or incurred is accrued in 'Interest income' or 'Interest expense', respectively, using the effective interest rate (EIR), while dividend income is recorded in 'Other operating income' when the right to the payment has been established.

3.5 Held-to-maturity

Held-to-maturity financial investments are those which carry fixed or determinable payments and have fixed maturities and which the bank has the intention and ability to hold to maturity. After initial measurement, held-to-maturity financial investments are subsequently measured at amortised cost using the effective interest rate method, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The amortisation is included in 'Interest income' in the statement of comprehensive income. The losses arising from impairment of such investments are recognised in the statement of comprehensive income.

If the bank were to sell or reclassify more than an insignificant amount of held-to-maturity investments before maturity (other than in certain specific circumstances), the entire category would be tainted and would have to be reclassified as available-for-sale. Furthermore, the bank would be prohibited from classifying any financial asset as held to maturity during the following two years.

3.6 Available-for-sale investments

Available-for-sale investments include equity and debt securities. Equity investments classified as available-for-sale are those which are neither classified as held-for-trading nor designated at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in the market conditions.

The bank has not designated any loans or receivables as available-for-sale.

After initial measurement, available-for-sale financial investments are subsequently measured at fair value, unless fair value cannot be reliably determined in which case they are measured at cost less impairment. Fair value changes are reported as a separate component of equity until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment, the cumulative gain or loss previously reported as "cumulative changes in fair value" within equity, is included in the statement of profit or loss for the year. Interest earned whilst holding available-for-sale financial investments is reported as interest income using the EIR. Dividends earned whilst holding available-for-sale financial investments are recognised in the statement of profit or loss as 'Other operating income' when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the profit or loss for the year in 'Impairment losses on available-for-sale financial investments' and removed from the 'Available-for-sale reserve'.

3.7 Derivative financial instruments and hedging activities

Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. The bank designates certain derivatives as either:

(i) hedges of the fair value of recognised assets or liabilities or a firm commitment (fair value hedge);

(ii) hedges of a particular risk associated with a recognised asset or liability or a highly probable forecast transaction (cash flow hedge); or

(iii) hedges of a net investment in a foreign operation (net investment hedge).

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.7 Derivative financial instruments and hedging activities (Continued)

The bank makes use of derivative instruments to manage exposures to interest rate, foreign currency and credit risks, including exposures arising from highly probable forecast transactions and firm commitments. In order to manage particular risks, the bank applies hedge accounting for transactions which meet specified criteria. Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any such derivative instruments are recognised immediately in the statement of comprehensive income within 'Other operating income'.

At inception of the hedge relationship, the bank formally documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the risk management objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship at inception and ongoing basis.

At each hedge effectiveness assessment date, a hedge relationship must be expected to be highly effective on a prospective

basis and demonstrate that it was effective (retrospective effectiveness) for the designated period in order to qualify for hedge accounting. A formal assessment is undertaken by comparing the hedging instrument's effectiveness in offsetting the changes in fair value or cash flows attributable to the hedged risk in the hedged item, both at inception and at each quarter end on an ongoing basis. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable the hedged risk during the period for which the hedge is designated were offset by the hedging instrument in a range of 80% to 125% and were expected to achieve such offset in future periods. Hedge ineffectiveness is recognised in the profit or loss in 'Other operating income'. For situations where the hedged item is a forecast transaction, the bank also assesses whether the transaction is highly probable and an exposure to variations in cash flows that could ultimately affect the statement of comprehensive income.

Fair value hedges

For designated and qualifying fair value hedges, the cumulative change in the fair value of a hedging derivative is recognised in the profit or loss in other operating income. Meanwhile, the cumulative change in the fair value of the hedged item attributable to the risk hedged is recorded as part of the carrying value of the hedged item in the statement of financial position and is also recognised in the profit or loss in other operating income. If the hedging instrument expires or is sold, terminated or exercised, or where the hedge no longer meets the criteria for hedge accounting, the hedge relationship is discontinued prospectively. For hedged items recorded at amortised cost, the difference between the carrying value of the hedged item on termination and the face value is amortised over the remaining term of the original hedge using the recalculated EIR method. If the hedged item is derecognised, the unamortised fair value adjustment is recognised immediately in the profit or loss.

Cash flow hedges

For designated and qualifying cash flow hedges, the effective portion of the cumulative gain or loss on the hedging instrument is initially recognised directly in equity in the cash flow hedge reserve. The ineffective portion of the gain or loss on the hedging instrument is recognised immediately in other operating income in the profit or loss.

When the hedged cash flow affects the profit or loss, the gain or loss on the hedging instrument is recorded in the corresponding income or expense line of the profit or loss. When the forecast transaction subsequently results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously recognised in the other comprehensive income are removed from the reserve and included in the initial cost of the asset or liability.When a hedging instrument expires, or is sold, terminated, exercised, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss that has been recognised in other comprehensive income at that time remains in other comprehensive income and is recognised when the hedged forecast transaction is ultimately recognised in the profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in other comprehensive income is immediately transferred to the profit or loss.

3.8 Due from banks and loans and advances to customers

Due from banks and loans and advances to customers are financial assets with fixed or determinable payments and fixed maturities that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale. After initial measurement, amounts due from banks and loans and advances to customers are subsequently measured at amortised cost using the effective interest rate method, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the effective interest rate. The amortisation is included in 'Interest income' in the profit or loss for the year. The losses arising from impairment are recognised in the profit or loss for the year in 'Credit loss expense'.

Notes to the Financial Statements
For the year ended 31 December 2017

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.9 Determination of fair values

A number of the bank's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on a number of accounting policies and methods. Where applicable, information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability. Details are set out in note 33.

3.9 Determination of fair values (Continued)

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible to the bank.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements on a recurring basis, the bank determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

At each reporting date, the bank analyses the movements in the values of assets and liabilities which are required to be re-measured or re-assessed as per the bank's accounting policies. For this analysis, the bank verifies the major inputs applied in the latest valuation by agreeing the information in the Valuation computation to contracts and other relevant documents.

The bank also compares each the changes in the fair value of each asset and liability with relevant external sources to determine whether the change is reasonable.

For the purpose of fair value disclosures, the bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

3.10 Premises and equipment

Premises and equipment are initially recorded at cost or deemed cost. Revaluations of buildings are carried out every five years on an open market value for existing use basis by an independent valuer. Net surpluses arising on revaluation are credited to a revaluation reserve, except that a revaluation increase is recognised as income to the extent that it reverses a revaluation decrease of the same asset previously recognised as an expense.

A decrease as a result of a revaluation is recognised as an expense, except that it is charged directly against any related revaluation surplus to the extent that the decrease does not exceed the amount held in the revaluation surplus in respect of that same asset. On disposal the related revaluation surplus is credited to retained earnings.

Land and capital work in progress are stated at cost and tested for impairment, if any. Depreciation is provided on a straight-line basis over the estimated useful lives of all premises and equipment other than freehold land, which is deemed to have an indefinite life, and capital work in progress.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.10 Premises and equipment (Continued)

The rates of depreciation are based upon the following estimated useful lives:

Buildings on freehold land	25 to 40 years
Leasehold improvements	Over the lease terms 3 to 10 years
Motor vehicles	4 years
Furniture	3 to 10 years
Equipment	5 to 20 years

The assets' residual values, useful lives and depreciation methods are reviewed and adjusted if appropriate at each statement of financial position date.

3.11 Derecognition of financial assets and financial liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired; or
- the bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and
- Either (a) the bank has transferred substantially all the risks and rewards of the asset, or (b) the bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the bank's continuing involvement in the asset. In that case, the bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the bank has retained. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the bank could be required to repay.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss for the year.

3.12 Collateral pending sale

The bank occasionally acquires real estate in settlement of certain loans and advances. Real estate is stated at the lower of the net realisable value of the related loans and advances and the current fair value of such assets. Gains or losses on disposal, and unrealised losses on revaluation, are recognised in the profit or loss for the year.

3.13 Deposits

All money market and customer deposits are carried at amortised cost using EIR.

3.14 Other borrowed funds

Other borrowings including subordinate private placements are recognised initially at their issue proceeds. Borrowings are subsequently stated at amortised cost; any difference between proceeds, net of transaction costs, and the redemption value is recognised in the profit or loss over the period of the borrowings using EIR.

3.15 Taxation – current and deferred

Taxation is provided for based on the relevant tax laws of the respective countries, in which the bank operates.

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the profit or loss for the year except to the extent that it relates to items recognised directly to other comprehensive income, in which case it is recognised in equity.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.19 Impairment of financial assets (Continued)

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is calculated using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

3.16 Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the bank and accordingly are not included in these financial statements.

3.17 Financial guarantees

In the ordinary course of business, the bank gives financial guarantees. Financial guarantees are initially recognised in the financial statements at fair value, in "other liabilities". Subsequent to initial recognition, the bank measures such guarantees at the higher of the initial fair value less, when appropriate, cumulative amortisation calculated to recognise the fee in the profit or loss for the year in "Net fees and commission income" over the term of the guarantee, and the best estimate of the expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the profit or loss for the year. Any financial guarantee liability remaining is recognised in the statement of comprehensive income when the guarantee is discharged, cancelled or expires.

3.18 Provisions

Provisions are recognised when the bank has a present obligation (legal or constructive) arising from a past event and the costs to settle the obligation are both probable and able to be reliably measured.

3.19 Impairment of financial assets

The bank assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults. If such evidence exists, the impairment loss is recognised in the profit or loss for the year.

Due from banks and loans and advances to customers

For amounts due from banks and loans and advances to customers carried at amortised cost, the bank first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the profit or loss for the year. Interest income continues to be accrued on the reduced carrying amount based on the original effective interest rate of the asset. Loans together with the associated allowance are written off

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.19 Impairment of financial assets (Continued)

when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the 'Recoveries from loans and advances written off'.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the bank's internal credit grading system that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, payment status, or other factors that are indicative of incurred losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Renegotiated loans
Where possible, the bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Held-to-maturity financial investments
For held-to-maturity investments the bank assesses individually whether there is objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced and the amount of the loss is recognised in the profit or loss for the year.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognised, any amounts formerly charged are credited to the 'Impairment losses on financial investments'.

Available-for-sale financial investments
For available-for-sale financial investments, the bank assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. For this purpose significant means 35% below cost, and prolonged mean quoted prices remaining or below cost for a period of 12 continuous months. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the profit or loss – is removed from equity and recognised in the profit or loss for the year. Impairment losses on equity investments are not reversed through the profit or loss; increases in their fair value after impairment are recognised directly in equity.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. Interest continues to be accrued at the original effective interest rate on the reduced carrying amount of the asset and is recorded as part of 'Interest income'. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the profit or loss, the impairment loss is reversed through the profit or loss.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.20 Perpetual Bond

The bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instrument. The bank's perpetual bonds are not redeemable by holders and bear an entitlement to distribution that is non-cumulative and at the discretion of the board of directors. Accordingly, they are presented as component within equity.

3.21 Offsetting

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

3.22 Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

Interest and similar income and expense
For all financial instruments measured at amortised cost, interest bearing financial assets classified as available for-sale and financial instruments designated at fair value through profit or loss, interest income or expense is recorded using the EIR, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original EIR and the change in carrying amount is recorded as 'Other operating income'.

Fee and commission income
The bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

Fee income earned from services that are provided over a certain period of time

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees.

Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the EIR on the loan. When it is unlikely that a loan will be drawn down, the loan commitment fees are recognised over the commitment period on a straight line basis.

Fee income from providing transaction services
Fees arising from negotiating or participating in the negotiation of a transaction for a third party, such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses, sale of insurance products are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

Dividend income

Dividend income is recognised when the bank's right to receive the payment is established.

3.23 Repurchase and resale agreements

Assets sold with a commitment to repurchase (repos) at a specified future date are recognised in the statement of financial position and are measured in accordance with accounting policies for trading securities or investment securities. The counter party liability for amounts received under these agreements is included in due to banks and other financial institutions. The difference between sale and repurchase price is treated as interest expense and accrued over the life of the repo agreement. Assets purchased with a corresponding commitment to resell at a specified future date (reverse repos) are not recognised in the statement of financial position and the amounts paid under these agreements are included in deposits with banks and other financial institutions. The difference between purchase and resale price is treated as interest income and accrued over the life of the reverse repo agreement.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

3.24 Leases

Operating lease payments are recognised as an expense in the statement of comprehensive income on a straight-line basis over the lease term.

3.25 Staff terminal benefits

The terminal benefits for employees in Oman are provided in accordance with the Sultanate of Oman's labour law. The end of service benefits for employees in UAE are provided for in accordance with the employees' contracts of employment and applicable requirements of the UAE labour laws. For Egyptian employees the terminal benefits are provided in accordance with the Egyptian social security law.

3.26 Segment reporting

The bank's segmental reporting is based on the following operating segments: retail banking, wholesale banking, commercial banking, head office and islamic. Segment results are reported to the Chief Executive Officer of the bank, (being the chief operating decision maker) and include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

3.27 Dividend on ordinary shares

Dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the bank's shareholders. Interim dividends are deducted from equity when they are paid.

Dividends for the year that are approved after the balance sheet date are dealt with as an event after the balance sheet date.

3.28 Directors' remuneration

The board of directors' remuneration is accrued within the limits specified by the Capital Market Authority and the requirements of the Commercial Companies Law of the Sultanate of Oman.

3.29 Impairment of non-financial assets

The carrying amount of the bank's non-financial assets, other than investment property and deferred tax assets are reviewed at each reporting date to determine whether there is any indication whether there is any indication of impairment. An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is reversed, only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss has been recognised.

3.30 Earnings per share

The bank presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprises convertible notes.

3.31 Foreign currency translation

(i) Transactions in foreign currencies are translated into Rial Omani at exchange rates ruling at the value dates of the transactions.

(ii) Monetary assets and liabilities denominated in foreign currencies are translated into Rial Omani at exchange rates ruling at the reporting date. The foreign currency gain or loss on monetary items is the difference between amortised costs in the Rial Omani at the beginning of the period, adjusted for effective interest and payments during the period and the amortised costs in foreign currency translated at the exchange rate at the end of the period. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of comprehensive income, except when deferred in other comprehensive income as qualifying cash flow hedges and qualifying net investment hedges.

(iii) Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to Rial Omani at the exchange rate at the date that the fair value was determined. Translation differences on non-monetary financial assets and liabilities such as equities held at fair value through profit or loss are recognised in profit or loss as part of the fair value gain or loss. Translation differences on non-monetary financial assets, such as equities classified as available-for-sale, are included in other comprehensive income.

3.32 Acceptances

Acceptances are disclosed on the statement of financial position under other assets with corresponding liability disclosed under other liabilities. Therefore, there is no off-balance sheet commitment for acceptances.

Notes to the Financial Statements
For the year ended 31 December 2017

4. CASH AND BALANCES WITH CENTRAL BANKS

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
121,005	**133,449**	Cash	**51,378**	46,587
657	**621**	Treasury bills with Central Banks	**239**	253
-	**20,418**	Certificate of Deposit with Central Banks	**7,861**	-
1,205,855	**839,307**	Other balances with Central Banks	**323,133**	464,254
1,327,517	**993,795**	**Cash and cash equivalents**	**382,611**	511,094
1,299	**1,299**	Capital deposit with Central Bank of Oman	**500**	500
1,328,816	**995,094**	**Cash and balances with Central Banks**	**383,111**	511,594

(i) At 31 December 2017, cash and balances with Central Bank of Oman included balances with the Central Bank of Oman amounting to RO 500,000 (2016: RO 500,000) as capital deposit. This cannot be withdrawn without the Central Bank of Oman approval.

(ii) Minimum cash reserve to be maintained with Central Bank of Oman as of 31 December 2017 amounted to RO 76 million (2016: RO 72 million).

5. DUE FROM BANKS AND OTHER MONEY MARKET PLACEMENTS (NET)

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
65,501	**49,000**	Loans and advances to banks	**18,865**	25,218
145,657	**193,260**	Placement with banks	**74,405**	56,078
88,577	**118,166**	Demand balances	**45,494**	34,102
299,735	**360,426**	**Due from banks and other money market placement**	**138,764**	115,398
(177)	**(244)**	Less: allowance for credit losses	**(94)**	(68)
299,558	**360,182**	**Net due from banks and other money market placement**	**138,670**	115,330

6. LOANS, ADVANCES AND FINANCING ACTIVITIES FOR CUSTOMERS (NET)

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
227,062	**259,714**	Overdrafts	**99,990**	87,419
3,478,474	**3,533,208**	Personal loans	**1,360,285**	1,339,213
2,983,466	**3,144,868**	Other loans	**1,210,774**	1,148,634
313,782	**152,805**	Loans against trust receipts	**58,830**	120,806
187,595	**105,254**	Bills discounted	**40,523**	72,224
7,190,379	**7,195,849**	**Gross loans and advances**	**2,770,402**	2,768,296
(221,745)	**(261,776)**	Allowance for credit losses	**(100,784)**	(85,372)
(32,839)	**(40,902)**	Reserved interest	**(15,747)**	(12,643)
6,935,795	**6,893,171**	**Net loans and advances**	**2,653,871**	2,670,281

6. LOANS, ADVANCES AND FINANCING ACTIVITIES FOR CUSTOMERS (NET) (Continued)

The movement in the allowance for credit losses and reserved interest accounts is set out below:

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
		Allowance for credit losses		
199,332	221,745	Balance at beginning of the year	85,372	76,743
51,029	65,229	Provided during the year	25,113	19,646
(5,268)	(2,426)	Released/recovered during the year	(934)	(2,028)
(22,945)	(22,777)	Written off during the year	(8,769)	(8,834)
(403)	5	Translation difference	2	(155)
221,745	261,776	Balance at end of the year	100,784	85,372
		Reserved interest		
29,774	32,839	Balance at beginning of the year	12,643	11,463
10,143	14,992	Reserved during the year	5,772	3,905
(1,405)	(5,384)	Released/recovered during the year	(2,073)	(541)
(5,545)	(1,545)	Written off during the year	(595)	(2,135)
(128)	-	Translation difference	-	(49)
32,839	40,902	Balance at end of the year	15,747	12,643

A further analysis of allowances for credit losses is set out below:

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
122,151	166,083	Specific impairment	63,942	47,028
99,594	95,693	Collective impairment	36,842	38,344
221,745	261,776		100,784	85,372

All loans and advances require payment of interest based on agreed tenors, some at fixed rates and others at rates that re-price prior to maturity. At 31 December 2017, impaired loans on which interest is not being accrued or where interest has been reserved amounted to RO 113 million – USD 294 million (2016 – RO 74 million – USD 192 million).

During the year, the bank has written-off fully provided loans and advances amounting to RO 9 million – USD 24.3 million (2016: RO 11 million – USD 28.5 million) against impairment provisions where the bank believes the possibility of a recovery is low. The bank will continue to pursue the recovery of these loans through all possible means and any future recovery from these written-off loans will be recognised in the profit or loss for the year.

Concentrations of credit risk arise when a number of counter parties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be affected similarly by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the bank's performance to developments affecting a particular industry or geographic location.

6. LOANS, ADVANCES AND FINANCING ACTIVITIES FOR CUSTOMERS (NET) (Continued)

The table below analyses the concentration of gross loans and advances by various sectors.

Total 2016 USD'000	Total 2017 USD'000		Total 2017 RO'000	Total 2016 RO'000
3,478,474	3,533,207	Personal	1,360,285	1,339,213
751,488	690,314	Service	265,771	289,323
631,647	502,174	Construction	193,337	243,184
583,831	496,579	Manufacturing	191,183	224,775
405,852	490,504	Financial institutions	188,844	156,253
108,156	431,816	Electricity, gas and water	166,249	41,640
396,821	379,699	Wholesale and retail trade	146,184	152,776
326,936	275,624	Others	106,115	125,870
147,797	199,455	Mining and quarrying	76,790	56,902
217,501	148,865	Import trade	57,313	83,738
120,642	30,166	Transport and communication	11,614	46,447
18,564	14,901	Agriculture	5,737	7,147
2,670	2,545	Government	980	1,028
7,190,379	7,195,849	Total Gross Loans	2,770,402	2,768,296

The geographic distribution of loans and advances to customers, based on the location of the borrower is as follows:

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
6,524,971	6,802,374	Sultanate of Oman	2,618,914	2,512,114
579,169	369,969	United Arab Emirates	142,438	222,980
403	392	Egypt	151	155
85,836	23,114	Others	8,899	33,047
7,190,379	7,195,849	Total	2,770,402	2,768,296

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7. FINANCIAL INVESTMENTS

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
		A. Held for trading		
		Quoted investments- Oman		
168,156	**143,431**	Government Development Bonds	**55,221**	64,740
-	**1,429**	Banking and investment sector	**550**	-
776	**-**	Equities	**-**	299
168,932	**144,860**		**55,771**	65,039
		Quoted investments- Foreign		
1,582	**-**	Equities	**-**	609
170,514	**144,860**	Total held for trading	**55,771**	65,648
		B. Available-for-sale		
		Quoted investments- Oman		
2,260	**-**	Banking and investment sector	**-**	870
366	**5,904**	Manufacturing sector	**2,273**	141
35,875	**54,704**	Service sector	**21,061**	13,812
-	**10,117**	Government Development Bonds	**3,895**	-
38,501	**70,725**		**27,229**	14,823
		Quoted investments- Foreign		
862	**6,602**	Banking and investment sector	**2,542**	332
9,356	**-**	Service sector	**-**	3,602
10,218	**6,602**		**2,542**	3,934
		Unquoted investments		
21,701	**19,345**	Banking and investment sector	**7,448**	8,355
9,047	**-**	Manufacturing sector	**-**	3,483
912	**886**	Service sector	**341**	351
31,660	**20,231**		**7,789**	12,189
80,379	**97,558**	**Total available-for-sale**	**37,560**	30,946
		C. Held-to-maturity		
		Quoted investments- Oman		
49,023	**199,963**	Government Development Bonds	**76,986**	18,874
15,000	**15,000**	Manufacturing sector	**5,775**	5,775
64,023	**214,963**		**82,761**	24,649
		Quoted investments- Overseas		
5,130	**5,112**	Banking and investment sector	**1,968**	1,975
13,416	**13,143**	Government Development Bond	**5,060**	5,165
18,546	**18,255**		**7,028**	7,140
82,569	**233,218**	**Total held-to-maturity**	**89,789**	31,789
333,462	**475,636**	**TOTAL FINANCIAL INVESTMENTS**	**183,120**	128,383

7. FINANCIAL INVESTMENTS (Continued)

Included under unquoted available-for-sale investments are investments with a value of RO 0.46 million – USD 1.2 million (2016 – RO 3.92 million – USD 10.18 million), which are carried at cost, less any impairment losses, due to the unpredictable nature of future cash flows and the lack of other suitable methods for arriving at a reliable fair value. All other available-for-sale investments are carried at fair value.

Details of impairment movement

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
5,166	**5,711**	Balance at beginning of the year	**2,199**	1,989
545	**1,787**	Provided during the year	**688**	210
5,711	**7,498**	Balance at end of the year	**2,887**	2,199

During the year, the bank has recorded RO 0.69 million – USD 1.79 million (2016 RO 0.21 million – USD 0.52 million) as impairment losses against its available-for-sale investments. The impairment loss on available-for-sale investments is recognised in view of either a significant or prolonged decline in the fair value of the investment below cost. A decline in value of security below its cost over thirty five percent is considered significant. Further, a decline in value of security below its cost for a continuous period of twelve months is considered prolonged.

Details of significant investments

Details of investments exceeding 10% of the carrying value of the bank's investment portfolio are as follows:

Bank's portfolio %	Carrying value USD'000		Bank's portfolio %	Carrying value RO'000
		2017		
74.3%	353,511	**Government Development Bonds-Oman**	%74.3	136,102
		2016		
65.1%	**217,179**	Government Development Bonds-Oman	65.1%	**83,614**

8. PREMISES AND EQUIPMENT

	Freehold land and buildings and leasehold improvements	Motor vehicles, furniture and equipment	Capital work in progress	Total
	RO'000	RO'000	RO'000	RO'000
Reconciliation of carrying amount:				
Balance as at 1 January 2017, net of accumulated				
depreciation	12,492	7,900	25,953	46,345
Additions	3,325	705	19,650	23,680
Disposals	-	(11)	(10)	(21)
Transfers	36,514	7,019	(43,533)	-
Translation difference	3	-	-	3
Depreciation	(1,085)	3,127	-	(4,212)
Balance at 31 December 2017, net of	**51,249**	**12,486**	**2,060**	**65,795**
accumulated depreciation				
At cost	62,353	41,420	2,060	105,833
At revaluation	4,385	-	-	4,385
Accumulated depreciation	(15,489)	(28,934)	-	(44,423)
Net carrying value at 31 December 2017	**51,249**	**12,486**	**2,060**	**65,795**
Net carrying value at 31 December 2017 – USD'000	**133,114**	**32.431**	**5,351**	**170,896**
At cost 31 December 2016	23,108	34,333	25,953	83,394
At revaluation	4,385	-	-	4,385
Accumulated depreciation	(15,001)	(26,433)	-	(41,434)
Net carrying value at 31 December 2016	12,492	7,900	25,953	46,345
Net carrying value at 31 December 2016– USD'000	32,447	20,520	67,410	120,377

During the year, the bank has capitalised its new head office building. Land and buildings above have a net carrying value of RO 49.77 million-USD 129.27million, (2016 – RO 10.74 million- USD 27.89 million) out of which freehold land at a cost of RO 8.56 million – USD 22.22 million (2016 – RO 8.56 million – USD 22.22 million) is not depreciated and not re-valued.

The bank has a policy to revalue its buildings at the end of every five years. In accordance with Bank's policy, three buildings on freehold land were re-valued at their open market value by an independent professional valuer during 2015. Should the buildings on freehold land be carried at cost less depreciation, the net carrying amount would have been RO 39.32 million – USD 102.13 million (2016 –RO 0.12 million – USD 0.31 million).

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9. OTHER ASSETS

2016	**2017**		**2017**	2016
USD'000	**USD'000**		**RO'000**	RO'000
47,916	**42,475**	Interest receivable and others	**16,353**	18,447
21,810	**7,016**	Positive fair value of derivatives (note 34)	**2,701**	8,397
85,917	**65,384**	Customers' indebtedness for acceptances	**25,173**	33,078
2,149	**4,047**	Deferred tax (note 14)	**1,558**	828
157,792	**118,922**		**45,785**	60,750

10. DUE TO BANKS AND OTHER MONEY MARKET DEPOSITS

2016	**2017**		**2017**	2016
USD'000	**USD'000**		**RO'000**	RO'000
575,953	**317,073**	Borrowings	**122,073**	221,742
9,073	**9,569**	Other balances	**3,684**	3,493
585,026	**326,642**		**125,757**	225,235

11. CUSTOMERS' DEPOSITS AND UNRESTRICTED INVESTMENT ACCOUNTS

2016	**2017**		**2017**	2016
USD'000	**USD'000**		**RO'000**	RO'000
2,208,660	**2,281,309**	Current accounts	**878,304**	850,334
1,568,444	**1,513,041**	Savings accounts	**582,521**	603,851
2,455,003	**2,598,551**	Term deposits	**1,000,442**	945,176
6,232,107	**6,392,901**		**2,461,267**	2,399,361

12. EURO MEDIUM TERM NOTES

The bank issued a 5-year, USD 600 million Regulation S, bond under its Euro Medium Term Note (EMTN) programme with regional and international investors. The bonds are listed on the Irish Stock Exchange and are governed by English law. The carrying amount of EMTN is stated after taking into account the amount of MTM value of the fair value hedge (Refer note 34).

Notes to the Financial Statements
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13. OTHER LIABILITIES

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
102,799	112,647	Interest payable and others	43,369	39,578
4,603	4,756	Staff entitlements	1,831	1,772
85,917	65,384	Liabilities under acceptances	25,173	33,078
14,634	7,725	Negative fair value of derivatives (note 34)	2,974	5,634
207,953	190,512		73,347	80,062
		Staff entitlements are as follows:		
3,956	4,073	End of service benefits	1,568	1,523
647	683	Other liabilities	263	249
4,603	4,756		1,831	1,772
		Movement in the end of service benefits liability are as follows:		
4,062	3,956	Liability as at 1 January	1,523	1,564
919	1,353	Expense recognised in the statement of comprehensive income	521	354
(1,025)	(1,236)	End of service benefits paid	(476)	(395)
3,956	4,073	Liability as at 31 December	1,568	1,523

14. TAXATION

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
		Current tax expense		
20,205	20,371	Current year	7,843	7,779
(371)	(1,579)	Deferred tax adjustment	(608)	(143)
19,834	18,792		7,235	7,636

The bank is liable to income tax at the following rates:

- Sultanate of Oman: 15% of consolidated taxable income (2016: 12% on taxable profits above RO 30,000)
- United Arab Emirates: 20% of taxable income
- Egypt: 22.50% of taxable income

14. TAXATION (Continued)

Set out below is reconciliation between income tax calculated on accounting profits with income tax expense for the year:

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
164,714	133,146	Accounting profit	51,261	63,415
19,766	19,972	Tax at applicable rate	7,689	7,610
(41)	1,962	Non-deductible expenses	755	(16)
(2,115)	(4,025)	Tax exempt revenues	(1,549)	(814)
2,595	2,462	Others	948	999
20,205	20,371		7,843	7,779

The bank's liabilities for taxation in the Sultanate of Oman have been assessed up to the year ended 31 December 2011.

The tax assessments of the Egypt operations in respect of the different taxes applicable are at different stages of completion with the respective tax authorities. The bank's liability in respect of its branches in UAE has been agreed with the tax authorities up to 31 December 2016.

Tax liability

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
20,205	20,371	Income tax and other taxes – Current year	7,843	7,779
(969)	(70)	Income tax and other taxes – Prior years	(27)	(373)
19,236	20,291		7,816	7,406

Recognised deferred tax assets

Deferred tax assets are attributable to the following:

2,261	3,843	Deductible temporary differences relating to provisions and revaluation of buildings	1,480	871
(112)	204	Available-for-sale investments	78	(43)
2,149	4,047		1,558	828

Movement of deferred tax asset/(liability)

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
1,953	2,151	Balance at the beginning of the year	828	752
371	1,579	Created during the year	608	143
(174)	317	Tax effect of movement in available-for-sale investments during the year	122	(67)
2,150	4,047		1,558	828

15. SUBORDINATED DEBT

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
135,325	**127,532**	At 1 January	**49,100**	52,100
(7,793)	**(62,597)**	Repaid during the year	**(24,100)**	(3,000)
127,532	**64,935**		**25,000**	49,100

16. SHARE CAPITAL

The Authorised share capital of the bank is 2,000,000,000 shares of RO 0.100 each (2016 – 2,000,000,000 of RO each). At 31 December 2017, 1,548,520,338 shares of RO 0.100 each (2016 – 1,474,781,275 shares of RO 0.100 each) have been issued and fully paid.

As of 31 December 2017, the following shareholders held 10% or more of the bank's capital:

	Number of shares '000	% Holding
The Commercial Bank of Qatar	540,431	34.90%
Suhail Bahwan Group (Holdings) L.L.C	228,318	14.74%
Civil Service Employee Pension Fund	175,098	11.31%

The percentage shareholding is calculated based on the total shares of the bank outstanding at the reporting date.

17. SHARE PREMIUM

The share premium of RO 34.5 million (USD 89.5 million) represents the premium collected on issue of 10 million shares by the bank through a private placement for RO 4.45 (USD 11.56) per share. This was approved by the bank's shareholders at the bank's Extraordinary General Meeting held in 2005 at which time the face value of the bank's share was RO 1.

18. LEGAL RESERVE

The legal reserve, which is not available for distribution, is accumulated in accordance with the requirements of the Commercial Companies Law of Oman and the Union Law No. 10 of UAE. The annual appropriations must not be less than 10% of the profit for the year until such time that the respective reserve account balance amounts to at least one third of the share capital in Oman and half of the branch capital in UAE. At 31 December 2017, the legal reserve of Oman has reached one third of the issued capital.

19. OTHER NON-DISTRIBUTABLE RESERVES

	Available-for-sale reserve RO '000	Revaluation reserve RO '000	Subordinated debt reserve RO '000	Total RO '000
At 1 January 2017	1,111	4,385	40,700	46,196
Net movement on available-for-sale investments	(4,417)	-	-	(4,417)
Tax effect of net losses on available-for-sale financial investments	122	-	-	122
Impairment losses on available-for-sale investments already recognised in comprehensive income	688	-	-	688
Transfer to retained earnings	-	-	(24,100)	(24,100)
Transfer to subordinated debt reserve	-	-	5,000	5,000
At 31 December 2017	(2,496)	4,385	21,600	23,489
At 31 December 2017 – In USD'000	**(6,483)**	**11,390**	**56,103**	**61,010**

19. OTHER NON-DISTRIBUTABLE RESERVES (Continued)

(i)The revaluation reserve represents the surplus on revaluation of building and is not available for distribution until the related assets have been disposed off or used.

(ii)The subordinated debt reserve represents an annual transfer towards subordinated debt which is due to mature within the next five years period (note 15). The reserve is available for transfer back to retained earning upon maturity of the subordinated debt.

20. TIER 1 PERPETUAL BOND

The bank, in 2015 issued Perpetual Tier 1 Capital Securities (the "Tier 1 Securities"), listed on Irish Stock Exchange, amounting to USD 300,000,000 (RO 115,500,000).

The Tier 1 Securities constitute direct, unconditional, subordinated and unsecured obligations of the bank and are classified as equity in accordance with IAS 32: Financial Instruments – Classification. The Tier 1 Securities do not have a fixed or final maturity date. They are redeemable by the bank at its sole discretion on 18 November 2020 (the "First Call Date") or on any interest payment date thereafter subject to the prior consent of the Central Bank of Oman.

The Tier 1 Securities bear interest on their nominal amount from the issue date to the First Call Date at a fixed annual rate of 7.875% which is the aggregate of margin and 5 year mid-swap rate that was prevailing at the time of issuance. The mid-swap rate will be reset at end of every fifth year. Interest will be payable semi-annually in arrears and treated as deduction from equity. Interest is non-cumulative and payable at the bank's discretion.

These securities form part of Tier 1 Capital of the bank and comply with Basel-3 and Central Bank of Oman regulations (BM 1114).

21. DIVIDENDS PAID AND PROPOSED

The Board of Directors have proposed a cash dividend of RO 0.015 per share totalling RO 23.2 million (USD 0.039 per share totalling USD 60.3 million) and stock dividend of RO 0.005 per share totalling RO 7.7 million (USD 0.013 per share totalling USD 20.1 million) for the year ended 31 December 2017, which is subject to the approval of the shareholders at the Annual General Meeting to be held in March 2018.

At the Annual General Meeting held in March 2017, a cash dividend of RO 0.016 per share totalling RO 23.5 million (USD 0.030 per share totalling USD 61 million) and stock dividend of RO 0.005 per share totalling RO 7.4 million (USD 0.013 per share totalling USD 19.2 million) for the year ended 31 December 2016 was approved and subsequently paid.

22. CONTINGENT LIABILITIES AND COMMITMENTS

To meet the financial needs of customers, the bank enters into various irrevocable commitments and contingent liabilities. Even though these obligations may not be recognised on the statement of financial position, they do contain credit risk and are therefore part of the overall risk of the bank.

Credit related commitments include commitments to extend credit, standby letters of credit and guarantees, which are designed to meet the requirements of the bank's customers.

Commitments to extend credit represent contractual commitments to make loans and revolving credits. Commitments generally have fixed expiration dates or other termination clauses and require the payment of a fee. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements.

Standby letters of credit and guarantees commit the bank to make payments on behalf of customers' contingent upon the failure of the customer to perform under the terms of the contract.

22.1 Contingent liabilities

As of the reporting date, commitments on behalf of customers for which there were corresponding customer liabilities consisted of the following:

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
1,204,062	**947,844**	Guarantees	**364,920**	463,564
208,140	**213,473**	Documentary letters of credit	**82,187**	80,134
1,412,202	**1,161,317**		**447,107**	543,698

22. CONTINGENT LIABILITIES AND COMMITMENTS (Continued)

The table below analyses the concentration of contingent liabilities by economic sector

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
713,273	**563,142**	Construction	**216,810**	274,610
184,516	**191,103**	Wholesale and retail trade	**73,575**	71,039
61,125	**113,205**	Others	**43,584**	23,533
178,146	**111,609**	Manufacturing	**42,970**	68,586
165,379	**91,525**	Financial institutions	**35,237**	63,671
68,729	**53,458**	Service	**20,581**	26,461
19,653	**23,422**	Transport and communication	**9,017**	7,566
2,914	**9,334**	Mining & quarrying	**3,594**	1,122
17,242	**3,271**	Electricity, gas and water	**1,259**	6,638
700	**699**	Personal	**269**	270
525	**549**	Agriculture	**211**	202
1,412,202	**1,161,317**		**447,107**	543,698

Guarantees include an amount of RO 14.3 million towards performance and advance payment guarantees which have been invoked by the beneficiary. The bank, based on an independent legal advice obtained is confident of recovering the amount payable to the beneficiary from its customer and has initiated a legal action against this customer. The bank has not created any provision for impairment loss for these disputed sums from its customer.

Guarantees include RO 0.29 million – USD 0.75 million (Dec 2016: RO 0.4 million – USD 1 million) relating to non-performing loans.

22.2 Commitments

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
618,262	**422,927**	Undrawn commitment	**162,827**	238,031
53,865	**5,062**	Capital expenditure	**1,949**	20,738
5,943	**8,894**	Operating lease commitments	**3,424**	2,288
		Future minimum lease payments:		
2,899	**3,340**	Not later than one year	**1,286**	1,116
3,044	**5,554**	Later than one year and not later than five years	**2,138**	1,172
5,943	**8,894**		**3,424**	2,288

22.3 Branches

The bank has deposited in the countries concerned, the following amounts of capital as support for its overseas branches. These amounts cannot be withdrawn without the approval of the Central Banks of the countries concerned.

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
88,584	**88,584**	UAE branch	**34,105**	34,105
50,000	**50,000**	Egypt branches	**19,250**	19,250
138,584	**138,584**		**53,355**	53,355

22. CONTINGENT LIABILITIES AND COMMITMENTS (Continued)

22.4 Legal claims

By nature of the banking sector, litigation whether by or against the bank is expected. In order to properly manage such litigation, the bank has in place effective mechanism and controls. The bank does not have any major/material legal proceedings pending in a court of law in Oman or outside either instituted by or against the bank, other than normal cases filed by clients in the normal course of business. However, there are certain unresolved legal claims filed against the bank which are not expected to have any significant implication on the bank's financial statements. Similarly, there are some ongoing cases filed by the bank against its borrowers in the course of its normal business practice.

22.5 Fiduciary assets

The fair value of securities as of 31 December 2017 held on trust for customers amounts to RO 47.8 million –USD 124.1 million (2016 – RO 59.62 million –USD 154.85 million).

23.INTEREST INCOME

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
347,748	**366,972**	Interest from customers	**141,284**	133,883
6,686	**9,096**	Interest from banks	**3,502**	2,574
354,434	**376,068**		**144,786**	136,457

Interest bearing assets, other than investments earned interest at an overall effective annual rate of 5.20 % for the year ended 31 December 2017 (31 December 2016 – 4.90%).

24.INTEREST EXPENSE

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
75,483	**107,327**	Interest to customers	**41,321**	29,061
12,174	**15,831**	Interest to banks	**6,095**	4,687
11,956	**18,130**	Euro medium term notes	**6,980**	4,603
99,613	**141,288**		**54,396**	38,351

For the year ended 31 December 2017, the average overall effective annual cost of bank's funds was 1.95 % (2016 – 1.43%).

25.OTHER OPERATING INCOME

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
41,587	**50,647**	Fees and commission income	**19,499**	16,011
(16)	**(18)**	Fees and commission expense	**(7)**	(6)
41,571	**50,629**	Net fees and commissions	**19,492**	16,005
16,288	**13,122**	Service charges	**5,052**	6,271
4,447	**4,829**	Profit on sale of investments	**1,859**	1,712
12,808	**12,774**	Net gains from foreign exchange dealings	**4,918**	4,931
9,545	**13,810**	Income from bonds and others	**5,317**	3,675
1,969	**3,488**	Dividend income	**1,343**	758
3,107	**3,164**	Miscellaneous income	**1,218**	1,196
89,735	**101,816**		**39,199**	34,548

26. OTHER OPERATING EXPENSES

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
16,088	**15,953**	Establishment costs	**6,142**	6,194
40,032	**41,691**	Operating and administration costs	**16,051**	15,412
810	**870**	Directors' remuneration and sitting fees	**335**	312
56,930	**58,514**		**22,528**	21,918

27. RELATED PARTY TRANSACTIONS

In the ordinary course of business, the bank conducts transactions with certain of its directors and/or shareholders and companies over which they have significant interest. The aggregate amounts of balances with such related parties are as follows:

	2017			2016		
	Principal shareholders RO'000	**Others RO'000**	**Total RO'000**	Principal shareholders RO'000	Others RO'000	Total RO'000
Loans and advances	-	**138,697**	**138,697**	-	99,039	99,039
Customers' deposits	**2,730**	**38,548**	**41,278**	82,292	35,304	117,596
Due from banks	**156**	**9,625**	**9,781**	55	13,668	13,723
Due to banks	**427**	-	**427**	28,917	-	28,917
Subordinated debt	**14,500**	**3,000**	**17,500**	14,500	4,000	18,500
Letter of credit, guarantees and acceptance	**3,057**	**8,765**	**11,822**	118	5,348	5,466
Standby revolving credit facility	**77,000**	-	**77,000**	77,000	-	77,000
Risk indemnities received	-	-	-	422	-	422
Investment	**1,981**	-	**1,981**	1,981	-	1,981

27. RELATED PARTY TRANSACTIONS (Continued)

The statement of comprehensive income includes the following amounts in relation to transactions with related parties:

	2017			2016		
	Principal share holders RO'000	**Others RO'000**	**Total RO'000**	**Principal share holders RO'000**	**Others RO'000**	**Total RO'000**
Interest Income	**40**	**6,275**	**6,315**	-	3,165	3,165
Commission Income	**80**	**895**	**975**	74	56	130
Interest Expense	2,947	**1,096**	**4,043**	3,357	387	3,744
Other Expense	**-**	**445**	**445**	-	1,051	1,051

	2017			2016		
	Principal share holders USD'000	**Others USD'000**	**Total USD'000**	**Principal share holders USD'000**	**Others USD'000**	**Total USD'000**
Loans and advances	-	**360,252**	**360,252**	-	257,244	257,244
Customers' deposits	**7,091**	**100,125**	**107,216**	213,745	91,699	305,444
Due from banks	**405**	**25,000**	**25,405**	143	35,501	35,644
Due to banks	**1,109**	-	**1,109**	75,109	-	75,109
Subordinated debt	**37,662**	**7,792**	**45,455**	37,662	10,390	48,052
Letter of credit, guarantees and acceptance	**7,940**	**22,766**	**30,706**	306	13,891	14,197
Standby revolving credit facility	**200,000**	-	**200,000**	200,000	-	200,000
Risk indemnities received	-	-	-	1,096	-	1,096
Investment	**5,145**	-	**5,145**	4,982	-	4,982

	2017			2016		
	Principal share holders USD'000	**Others USD'000**	**Total USD'000**	**Principal share holders RO'000**	**Others USD'000**	**Total USD'000**
Interest income	**104**	**16,299**	**16,403**	-	**8,221**	**8,221**
Commission income	**208**	**2,325**	**2,531**	192	145	337
Interest expense	**7,655**	**2,847**	**10,502**	8,719	1,005	9,724
Other expenses	**-**	**1,156**	**1,156**	-	2,730	2,730

Details regarding senior management compensation are set out below:

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
		Salaries and other short term benefits		
8,143	**8,309**	- Fixed	**3,199**	3,135
3,766	**3,894**	- Discretionary	**1,499**	1,450
11,909	**12,203**		**4,698**	4,585

28.BASIC AND DILUTED EARNINGS PER SHARE

Earnings per share is calculated by dividing the profit for the year by the weighted average number of shares outstanding during the year as follows:

	2017 RO'000	2016 RO'000
Profit after tax	44,026	55,779
Less: Interest on tier 1 perpetual bond	(9,096)	(8,010)
Profit attributable to shareholders	34,930	47,769
Weighted average number of shares outstanding during the year (in '000s)	1,548,520	1,548,520
Earnings per share (RO)	RO 0.023	RO 0.031
	2017 USD'000	**2016 USD'000**
Profit after tax	114,353	144,880
Less: Interest on tier 1 perpetual bond	(23,626)	(20,805)
Profit attributable to shareholders	90,727	124,075
Weighted average number of shares outstanding during the year (in '000s)	1,548,520	1,548,520
Earnings per shawre (USD)	USD 0.06	USD 0.08

During the year 2017, the bank issued bonus shares amounting to RO 7.4 million at RO 0.005 per share (USD 0.013 per share totalling USD 19.2 million). As the issue was without any consideration, the number of ordinary shares outstanding before the event is adjusted for the proportionate change in the number of ordinary shares outstanding as if the event had occurred at the beginning of the earliest period presented.

No figure for diluted earnings per share has been presented, as the bank has not issued any instruments, which would have an impact on earnings per share when exercised.

29.CAPITAL ADEQUACY

The bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the bank's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision and adopted by the Central Bank of Oman in supervising the bank.

During the past year, the bank had complied in full with all its externally imposed capital requirements.

Capital management

The primary objectives of the bank's capital management are to ensure that the bank complies with externally imposed capital requirements and that the bank maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

The bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the bank may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. The Capital Management Policy was revised during the year to incorporate the regulatory changes.

The international standard for measuring capital adequacy is the risk asset ratio, which relates capital to balance sheet assets and off balance sheet exposures weighted according to broad categories of risk.

29. CAPITAL ADEQUACY (Continued)

The risk asset ratio calculated in accordance with the capital adequacy guidelines of the bank for International Settlement is as follows:

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
		Capital base		
1,021, 070	1,043,086	Common equity Tier 1 - shareholders' funds	401,588	393,112
300,000	300,000	Additional Tier 1 - capital	115,500	115,500
122,888	101,896	Tier 2 - subordinated debt and collective impairment provisions	39,230	47,312
1,443,958	1,444,982	Total capital base	556,318	555,924
		Risk weighted assets		
7,500,257	7,445,255	Credit risk	2,866,423	2,887,599
626,722	655,779	Operational risk	252,475	241,288
155,584	228,543	Market risk	87,989	59,900
8,282,563	8,329,577	Total risk weighted assets	3,206,887	3,188,787
12.3%	12.5%	CET 1 Ratio	12.5%	12.3%
16.0%	16.1%	Tier 1 Ratio	16.1%	16.0%
17.4%	17.3%	Risk asset ratio (Basel II norms)	17.3%	17.4%

30.RISK MANAGEMENT

Effective risk management is of primary importance for the bank. The bank's risk management process evaluates, monitors and manages the risks associated with the businesses the bank conducts in line with the defined risk appetite. The bank's key risks are credit risk, market risk, operational risk and strategic risk. The bank operates on the guiding principles of three lines of defense i.e. Business, Independent control functions and internal audit. The risk management function is headed by the CRO with a team of risk professionals to manage specific risk functions.

30.1 Credit Risk

Credit risk is the risk of potential loss in the event that the bank's customers, clients or counterparties fail to honour their financial and contractual obligations to the bank. Credit risk is one of the most significant risks for the bank. The bank has a robust credit risk framework and policies for each of the businesses it operates. The policies are aligned with the risk appetite and credit limits are set up based on the counter party risk rating, industry sector, and as per the guidelines of Central Bank of Oman.

Credit risk management

Credit Risk is managed within the regulatory requirements of Central Bank of Oman; the risk framework is provided in the Board approved Risk Charter and Credit Policies and Procedures. The policies and procedures are periodically reviewed to ensure alignment to the current best practices. Credit exposures are approved by delegated authorities based on the delegation by the Board and Board Risk Committee. The delegation of authorities is based on the size of the single obligor exposure, the credit quality (internal, external rating) as well as level of credit risk mitigation (collateral, guarantees, etc.) for the proposed exposures. For retail exposures, there is delegation of authority for handling exceptions to approved program lending. Control, monitoring and management of credit exposures and remedial management are done in coordination with respective Business Units as per established procedures. The risk management framework also includes policies with respect to problem recognition, early warning lists, watch lists, classification parameters and risk rating adjustments. The bank is contemplating an early warning trigger system based on predefined credit parameters and account behaviour. The bank also undertakes stress testing of its portfolio and potential credit costs in the event of a downgrade or default by its customers.

30. RISK MANAGEMENT (Continued)

30.1 Credit Risk (Continued)

Corporate credit

Corporate Credit Risk Division is responsible for independent assessment and control of the risks related to all Corporate, Business Banking, Financial Institutions as well as Small and Medium enterprise exposures. The credit risk associated with any corporate financing is assessed based on an analysis of the customer and the industry it operates in. The credit rating acts as a key factor in credit decisions at the time of approval and subsequent credit assessments. The Division reviews and assesses credit risk for proposed exposures prior to facilities being committed to customers by the concerned business units. Renewals and reviews of facilities are subject to the same process. Each proposal is also assessed with respect to established concentration limits for various economic sectors, countries, risk grades, etc. and deviations, if any are highlighted. The bank follows a risk adjusted return of capital model for benchmarking risk pricing and each credit proposal is also assessed based on internal benchmarks of required risk adjusted returns. The bank has implemented a customised Moody's Risk Analyst model for risk rating corporate borrowers. The bank maintains an accurate and consistent corporate credit rating for all its customers. The bank has introduced facility risk rating apart from customer credit rating so as to measure the appropriate loss given default associated with each credit.

In addition to formal annual credit risk reviews of each corporate facility, more frequent reviews are also undertaken for watch list accounts, early warning accounts, lower rated customers, public companies and large exposures. Further, the bank continues to undertake quarterly review of financial institutions and country portfolio including stress tests and review of adverse rating migrations and outlooks in line with best practices and regulatory guidelines. The bank also undertook a weekly review across all its business segments of early warning accounts, which showed signs of stress, and remedial action prescribed as necessary. The bank undertook sector review of its exposure to Real estate, Construction, Steel, Healthcare and lending against shares.

A comprehensive review of the Corporate Credit Portfolio is conducted on a quarterly basis and provided to the Senior Management and the Board Risk Committee. Salient areas covered in the review include:-

- Exposures downgraded/negatively migrated
- Weighted average credit grade profile
- Portfolio concentration/ performance
- Position of restructured exposures
- Position of past due exposures
- Exposures secured by equity
- Exposures to real estate and leasing sectors
- Syndicated exposures
- New relationships
- Exposures to senior members and non-resident borrowers
- Exposures to countries / financial institutions
- Clean lending and name lending exposures

The bank introduced prudent control measures for its UAE operations in line with the changing operating environment detailed below

- Revised business focus on Oman-UAE business corridor with emphasis on businesses sponsored by Omani or reputed UAE nationals.
- Enhanced Due diligence and strengthened KYC processes
- Revised Standard Operating Procedures in line with changing business needs.

Retail credit

Retail Credit Division manages the credit risk in the retail portfolio. Credit facilities are offered to retail customers primarily based on Product Programs approved by Risk Committee of the Board. The lending criteria for these programs are regularly reviewed and, if required revised, based on an on-going analysis of product performance and portfolio credit quality and perceived risk. Credit facilities outside the Product Programs are individually assessed by the Retail Credit Risk Division and recommended to the delegated authorities.

A review of the Retail Credit Portfolio is conducted on a quarterly basis and provided to the Management Risk Committee, and to the Board Risk Committee. Monthly management reports are also prepared and submitted to the CRO and to the Business Heads. Salient areas covered in the review include:

- Portfolio quality
- Management Summary of Delinquency and NPA trends (which includes product-wise delinquency analysis, vintage analysis, and delinquencies across various credit criteria, etc.)
- Projects undertaken / fulfilled during the quarter.

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For the year ended 31 December 2017

30. RISK MANAGEMENT (Continued)

30.1 Credit Risk (Continued)

System enhancements and continuous improvements have been made on all processes that are critical to improve quality of overall retail portfolio. The bank has a lending strategy through the adoption of pre-defined lending criteria and continuous monitoring of the portfolio, and has implemented a Credit application Scoring Module for its salary related loan portfolio to enhance the Retail Credit Risk framework.

Loan review mechanism

The bank has an independent Loan Review Mechanism Division (LRM) with a mandate for constantly evaluating the quality of the loan book, and the balance between risk and reward and to bring about qualitative improvements in credit administration. The division evaluates the effectiveness of loan administration, integrity of the credit grading process, assessment of general and specific loan loss provisions, portfolio quality, etc. In addition to the above the LRM team reviews the bank's effectiveness of approved internal controls and procedures to ensure robust and sound practices are being followed by all stake holders. LRM also performs independent ad hoc reviews, investigations and assessments as directed by management on areas of concern relating to the credit approval process and/or the analysis processes within the bank. Significant findings are reported to the CRO, the MRC and potentially to the BRC where warranted.

Risk mitigation policies

The bank manages, limits and controls concentrations of credit risk - in particular, with respect to individual counterparties and groups, and industries and countries. The bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored and reviewed periodically by the Management Credit Committee and Board Risk Committee.

Maximum exposure to credit risk

Gross maximum exposure 2016 USD'000	**Gross maximum exposure 2017 USD'000**		**Gross maximum exposure 2017 RO '000**	Gross maximum exposure 2016 RO '000
1,207,811	**861,645**	Balances with Central Banks	**331,733**	465,007
299,558	**360,182**	Due from banks and other money market placements(net)	**138,670**	115,330
6,935,795	**6,893,171**	**Loans, advances and financing activities for customers (net)**	**2,653,871**	2,670,281
333,462	**475,636**	Financial investments	**183,120**	128,383
133,833	**111,906**	Other assets	**43,084**	51,525
21,810	**7,016**	Derivatives	**2,701**	8,397
8,932,269	**8,709,556**	Total on balance sheet exposure	**3,353,179**	3,438,923
1,204,062	**947,844**	Guarantees	**364,920**	463,564
208,140	**213,473**	Documentary letters of credit	**82,187**	80,134
618,262	**341,109**	Undrawn commitment	**131,327**	238,031
2,030,464	**1,502,426**	Total off balance sheet exposure	**578,434**	781,729

The above table represents the maximum credit risk exposure to the bank at 31 December 2017 and 2016 without taking into account the collateral held or other credit enhancements. Management is confident that the bank has suitable policies to measure and control the credit risk. In addition credit risk is mitigated through collaterals in the form of mortgages and guarantees wherever required.

30. RISK MANAGEMENT (Continued)

30.1 Credit Risk (Continued)

An analysis of the credit quality of the bank's loan and advances is set out below:

	Performing loans (neither past due tor impaired)	Loans past due and not impaired	Non performing loans	Gross loans
	RO'000	RO'000	RO'000	RO'000
Balance as at 1 January 2017	2,503,590	190,843	73,863	2,768,296
Additions during the year	792,420	119,366	90,248	1,002,034
Attrition during the year	(771,416)	(177,329)	(41,819)	(990,564)
Written-off during the year	-	-	(9,364)	(9,364)
Balance as at 31 December 2017	2,524,594	132,880	112,928	2,770,402
Balance as at 31 December 2017 – USD'000s	6,557,388	345,143	293,319	7,195,850
Balance as at 31 December 2016	2,503,590	190,843	73,863	2,768,296
Balance as at 31 December 2016 – USD'000s	6,502,831	495,696	191,852	7,190,379

An ageing analysis of the bank's loans which are past due but not impaired is set out below:

	Loans in arrears 1-30 days	Loans in arrears 31-60 days	Loans in arrears 61-89 days	Total
	RO'000	RO'000	RO'000	RO'000
Loans and advances to customers at				
31 December 2017	36,853	55,612	40,415	132,880
31 December 2017 – USD'000s	95,722	144,447	104,974	345,143
31 December 2016	42,539	53,307	94,997	190,843
31 December 2016 – USD'000s	110,491	138,460	246,745	495,696

Collateral and other credit enhancements

The bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advanced, which is the common practice. The bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Charges over business assets such as premises, inventory and accounts receivable
- Lien on fixed deposits
- Cash margins
- Mortgages over residential and commercial properties
- Pledge of marketable shares and securities

The housing loans are secured by mortgage over the residential property.

The Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

It is the bank's policy to dispose of repossessed properties in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. In general, the bank does not occupy repossessed properties for business use.

30. RISK MANAGEMENT (Continued)

30.1 Credit Risk (Continued)

An analysis of the collateral held and other credit enhancement held against loan and advances granted is as follows:

	Performing loans (neither past due tor impaired)	Loans past due and not impaired	Non performing loans	Gross loans
	RO'000	RO'000	RO'000	RO'000
Collateral available	2,022,267	96,566	21,253	2,140,086
Guarantees available	1,390	-	-	1,390
Government soft loans*	923	-	2,579	3,502
Balance as at 31 December 2017	2,024,580	96,566	23,832	2,144,978
Balance as at 31 December 2017 – USD'000s	5,258,649	250,821	61,901	5,571,371
Balance as at 31 December 2016	1,625,605	101,665	74,739	1,802,009
Balance as at 31 December 2016 – USD'000s	4,222,351	264,065	194,127	4,680,543

* Government Soft Loans are guaranteed by the Government to the extent of the outstanding principal.

The amount of total secured loans and advances is less than the total value of collateral as stated above.

Impairment and provisioning policy

An assessment is made at each reporting date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the net present value of future anticipated cash flows, recognised in the statement of comprehensive income. In addition the bank creates collective provision.

A further analysis of the bank's non-performing loans in accordance with the classification requirements of Central Bank of Oman is as follows:

	Substandard	Doubtful	Loss	Total
	RO'000	RO'000	RO'000	RO'000
Balance as at 1 January 2017	8,879	21,516	43,468	73,863
Additions during the year	9,219	50,434	33,046	92,699
Attrition during the year	(5,559)	(34,029)	(4,682)	(44,270)
Written-off during the year	-	-	(9,364)	(9,364)
Balance as at 31 December 2017	12,539	37,921	62,468	112,928
Balance as at 31 December 2017 – USD'000s	32,569	98,496	162,255	293,320
Balance as at 31 December 2016	8,879	21,516	43,468	73,863
Balance as at 31 December 2016 – USD'000s	23,062	55,886	112,904	191,852

Movement of rescheduled loans:

	2017	2016
	RO'000	RO'000
Balance as at 1 January	70,676	60,682
Additions during the year	19,308	30,883
Attrition during the year	(28,494)	(20,889)
Balance as at 31December	61,490	70,676
Balance as at 31December – USD'000s	159,714	183,574

30. RISK MANAGEMENT (Continued)

30.2 Liquidity Risk

Liquidity risk is the risk that the bank will be unable to meet its payment obligations when they fall due under normal and stressed circumstances. To limit this risk, the management continuously looks for opportunities to diversify its funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The bank maintains liquidity by continually assessing, identifying and monitoring changes in funding needs required to meet strategic goals set in terms of the overall strategy. In addition the bank holds certain liquid assets as part of its liquidity risk management strategy.

The bank manages the liquidity risk based on the Central Bank of Oman guidelines and the Liquidity and Liquidity Contingency Policies, which are approved and periodically reviewed by the Board Risk Committee. Liquidity Risk position is monitored regularly through analysis of various reports, such as, Maturity of Assets and Liabilities, Liquidity Lines, Early Warning Indicators and Stock Ratios. Further, the bank also periodically conducts stress tests on liquidity based on market and bank specific events in line with Basel Committee recommendations. The liquidity position of the bank and stress test scenarios are regularly reviewed by the management and also discussed at the Board Risk Committee.

The Central Bank of Oman has issued guidelines on the implementation of Basel III liquidity framework which are Liquidity Coverage Ratio (LCR) and Net Stable Funding (NSFR).

The Net Stable Funding Ratio (NSFR) is a longer term structural ratio designed to address liquidity mismatches and reduce funding risk over a one year horizon. It is effective January 2018, with a minimum ratio of 100% as per the regulatory guidance.

The residual maturity profile of the assets, liabilities and equity at **31 December 2017** is as follows:

	On demand within 3 months	3 to 12 months	Subtotal less than 12 months	1 to 5 years	Over 5 years	Subtotal over 12 months	Total
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Banks	323,582	25,475	349,057	17,907	16,147	34,054	383,111
Due from banks and other money market placements (net)	107,331	20,174	127,505	1,540	9,625	11,165	138,670
Loans, advances and financing activities for customers (net)	366,100	295,458	661,558	628,930	1,363,383	1,992,313	2,653,871
Financial investments	95,070	1,972	97,042	16,065	70,013	86,078	183,120
Premises and equipment	-	-	-	-	65,795	65,795	65,795
Other assets	40,372	4,554	44,926	859	-	859	45,785
Total assets	932,455	347,633	1,280,088	665,301	1,524,963	2,190,264	3,470,352
Due to banks and other money market deposits	83,379	3,878	87,257	38,500	-	38,500	125,757
Customers' deposits and unrestricted investment accounts	694,205	766,791	1,460,996	540,763	459,508	1,000,271	2,461,267
Euro medium term notes	-	-	-	230,906	-	230,906	230,906
Other liabilities	68,657	3,782	72,439	908	-	908	73,347
Taxation	7,816	-	7,816	-	-	-	7,816
Subordinated debt	-	7,000	7,000	18,000	-	18,000	25,000
Shareholders' equity	-	-	-	-	430,759	430,759	430,759
Tier 1 perpetual bonds	-	-	-	-	115,500	115,500	115,500
Total liabilities and shareholders' equity	854,057	781,451	1,635,508	829,077	1,005,767	1,834,844	3,470,352

30. RISK MANAGEMENT (Continued)

30.2 Liquidity Risk (Continued)

	On demand within 3 months	3 to 12 months	Subtotal less than 12 months	1 to 5 years	Over 5 years	Subtotal over 12 months	Total
	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
Cash and balances with Central Banks	840,473	66,169	906,642	46,512	41,940	88,452	995,094
Due from banks and other money market placements (net)	278,782	52,400	331,182	4,000	25,000	29,000	360,182
Loans, advances and financing activities for customers (net)	950,909	767,423	1,718,332	1,633,584	3,541,255	5,174,839	6,893,171
Financial investments	246,935	5,122	252,057	41,727	181,852	223,579	475,636
Premises and equipment	-	-	-	-	170,896	170,896	170,896
Other assets	104,862	11,829	116,691	2,231	-	2,231	118,922
Total assets	2,421,961	902,943	3,324,904	1,728,054	3,960,943	5,688,997	9,013,901
Due to banks and other money market deposits	216,569	10,073	226,642	100,000	-	100,000	326,642
Customers' deposits and unrestricted investment accounts	1,803,130	1,991,665	3,794,795	1,404,579	1,193,527	2,598,106	6,392,901
Euro medium term notes	-	-	-	599,756	-	599,756	599,756
Other liabilities	178,331	9,823	188,154	2,358	-	2,358	190,512
Taxation	20,301	-	20,301	-	-	-	20,301
Subordinated debt	-	18,182	18,182	46,753	-	46,753	64,935
Shareholders' equity	-	-	-	-	1,118,854	1,118,854	1,118,854
Tier 1 perpetual bonds	-	-	-	-	300,000	300,000	300,000
Total liabilities and shareholders' equity	2,218,331	2,029,743	4,248,074	2,153,446	2,612,381	4,765,827	9,013,901

30. RISK MANAGEMENT (Continued)

30.2 Liquidity Risk (Continued)

The maturity profile of the assets, liabilities and equity at 31 December 2016 is as follows:

	On demand within 3 months	3 to 12 months	Subtotal less than 12 months	1 to 5 years	Over 5 years	Subtotal over 12 months	Total
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Bankst	411,741	41,628	453,369	31,522	26,703	58,225	511,594
Due from banks and other money market placements (net)	89,149	16,556	105,705	-	9,625	9,625	115,330
Loans, advances and financing activities for customers (net)	440,592	250,106	690,698	595,852	1,383,731	1,979,583	2,670,281
Financial investments	94,543	13,905	108,448	19,935	-	19,935	128,383
Premises and equipment	-	-	-	-	46,345	46,345	46,345
Other assets	56,309	3,870	60,179	571	-	571	60,750
Total assets	1,092,334	326,065	1,418,399	647,880	1,466,404	2,114,284	3,532,683
Due to banks and other money market deposits	114,075	107,281	221,356	3,879	-	3.879	225,235
Customers' deposits and unrestricted investment accounts	606,580	757,964	1,364,544	571,298	463,519	1,034,817	2,399,361
Euro medium term notes	-	-	-	233,105	-	233,105	233,105
Other liabilities	76,279	2,587	78,866	1,196	-	1,196	80,062
Taxation	7,406	-	7,406	-	-	-	7,406
Subordinated debt	-	24,100	24,100	25,000	-	25,000	49,100
Shareholders' equity	-	-	-	-	422,914	422,914	422,914
Tier 1 perpetual bonds	-	-	-	-	115,500	115,500	115,500
Total liabilities and shareholders' equity	804,340	891,932	1,696,272	834,478	1,001,933	1,836,411	3,532,683

	On demand within 3 months	3 to 12 months	Subtotal less than 12 months	1 to 5 years	Over 5 years	Subtotal over 12 months	Total
	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
Cash and balances with Central Banks	1,069,458	108,125	1,177,583	81,875	69,358	151,233	1,328,816
Due from banks and other money market placements (net)	231,555	43,003	274,558	-	25,000	25,000	299,558
Loans, advances and financing activities for customers (net)	1,144,395	649,626	1,794,021	1,547,668	3,594,106	5,141,774	6,935,795
Financial investments	245,566	36,117	281,683	51,779	-	51,779	333,462
Premises and equipment	-	-	-	-	120,377	120,377	120,377
Other assets	146,257	10,052	156,309	1,483	-	1,483	157,792
Total assets	2,837,231	846,923	3,684,154	1,682,805	3,808,841	5,491,646	9,175,800

30. RISK MANAGEMENT (Continued)

30.2 Liquidity Risk (Continued)

Due to banks and other money market deposits	296,299	278,652	574,951	10,075	-	10,075	585,026
Customers' deposits and unrestricted investment accounts	1,575,532	1,968,738	3,544,270	1,483,891	1,203,946	2,687,837	6,232,107
Euro medium term notes	-	-	-	605,468	-	605,468	605,468
Other liabilities	198,128	6,719	204,847	3,106	-	3,106	207,953
Taxation	19,236	-	19,236	-	-	-	19,236
Subordinated debt	-	62,597	62,597	64,935	-	64,935	127,532
Shareholders' equity	-	-	-	-	1,098,478	1,098,478	1,098,478
Tier 1 perpetual bonds	-	-	-	-	300,000	300,000	300,000
Total liabilities and shareholders' equity	2,089,195	2,316,706	4,405,901	2,167,475	2,602,424	4,769,899	9,175,800

Liquidity coverage ratio

The Liquidity coverage ratio (LCR) is a short time ratio designed to increase resilience against a liquidity shortage of up to 30 days. The LCR is computed as per CBO requirement under the circular BM1127 (BASEL III: Framework on Liquidity coverage ratio and LCR disclosure standards). It is applicable from January 1, 2015 with a minimum ratio of 60% and increasing by 10% every year thereafter till it reaches a minimum required level of 100% on 1 January, 2019.

Total Weighted Value (average)	Total Unweighted Value (average)		Total Unweighted Value (average)	Total Weighted Value (average)
USD'000	USD'000		RO'000	RO'000
1,275,225	-	HIGH QUALITY LIQUID ASSETS	-	490,962
1,275,225	-	Total High Quality Liquid Assets (HQLA)	-	490,962
		Cash outflows		
108,106	1,860,146	Retail deposits and deposits from small business customers of which:	716,156	41,621
77,909	1,558,173	Stable deposits	599,897	29,995
30,197	301,972	Less stable deposits	116,259	11,626
838,867	2,405,464	Unsecured wholesale funding, of which: Operational deposits (all counterparties) and deposits in networks of cooperative banks	926,104	322,964
8,427	84,274	Additional requirements, of which Credit and liquidity facilities	32,445	3,245
68,116	1,276,068	Other contingent funding obligations	491,286	26,225
1,023,516	-	TOTAL CASH OUTFLOWS	-	394,054
		Cash Inflows		
539,875	752,440	Inflows from fully performing exposures	289,689	207,852
29,042	29,042	Other cash inflows	11,181	11,181
568,917	781,482	TOTAL CASH INFLOWS	300,870	219,033
1,275,225	-	TOTAL HIGH QUALITY LIQUID ASSETS	-	490,962
454,599	-	TOTAL NET CASH OUTFLOWS	-	175,021
280.52	-	LIQUIDITY COVERAGE RATIO (%)	-	280.52

30. RISK MANAGEMENT (Continued)

30.3 Market Risk

The bank is exposed to market risk, which is the risk that the fair value of the financial assets held by the bank will fluctuate due to changes in market prices. Market risk arises from changes in the fair value of open positions held in foreign exchange, interest rate, currency, equity, credit spreads, etc. Market risk is managed based on the Central Bank of Oman guidelines and the Market Risk Policy, which is approved and periodically reviewed by the Board Risk Committee. Stress tests are also conducted periodically incorporating adverse movements in equity value, foreign exchange, etc. and reviewed by the Management and Board Risk Committee.

The bank offers hedging products to its customers to hedge their genuine exposures, related to interest rate risk, foreign exchange risk and commodity risk. The counterparty credit risk exposures for such transactions (interest rate swaps, commodities contracts, currency forwards and options, etc.) are assessed based on the positive marked-to-market values of the contracts and the potential future exposures. The bank has adopted risk weightings in line with best practices to capture the credit risk related to these off-balance sheet exposures.

Equity risk

The proprietary equity positions are held in the 'Available-for-Sale' category. The market risk is monitored though daily mark-to-market reports which are circulated to the management and, if any, required actions are promptly taken. The portfolio is also monitored and managed as per the Investment Policy approved by the Board Risk Committee.

Interest rate risk

The principal market risk to which non-trading portfolio is exposed is the risk of loss from fluctuation in the future cash flows or fair values of financial instruments because of changes in market interest rates.

Interest rate risk arises from the possibility that changes in interest rates will affect future profitability or the fair values of financial instruments. The bank is exposed to interest rate risk as a result of mismatches of interest rate re-pricing of assets and liabilities.

Methods and assumptions used in preparing the sensitivity analysis: The methods for interest rate sensitivity analysis are Maturity Gap Analysis (which measures the interest rate sensitivity of earnings) and Duration (which measures the interest rate sensitivity of capital). These are in line with the BIS in its paper on 'Principles for the Management and Supervision of Interest Rate Risk' issued in July 2004.

Interest rate risk is managed by monitoring the sensitivity of the bank's financial assets and liabilities to various standardized interest rate shocks. Standardised shocks include a 100 basis point and 200 basis point parallel shifts in yield curves that are considered on a monthly basis. The impact of these shocks is analysed in the context of its impact on Earnings and Economic Value. The impact is compared against internal limits which have been formulated in line with the Central Bank of Oman and Basel Committee guidelines. The analysis is regularly reviewed by the Management and Board Risk Committee.

Earning impact of 200 basis points parallel shift in interest rate is provided below:

As at December 2017	200 bps increase	200 bps decrease
Earnings impact - RO'000s	7,151	(7,151)
Earnings impact - USD'000s	18,575	(18,575)

In addition, stress scenarios based on specific events or market disruptions are also analysed and presented at monthly ALCO meetings to estimate the impact on liquidity and earnings.

The bank has been consistently using the above methods/assumptions to conduct interest rate sensitivity analysis. The above sensitivity analyses are carried out at monthly rests and results thereof monitored against the in-house limits and the results are also actively deliberated at the ALCO meetings and presented to the Board Risk Committee.

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30. RISK MANAGEMENT (Continued)

30.3 Market Risk (Continued)

There have not been any significant changes in Interest Rate Risk management process in the bank during the year.

The bank's interest sensitivity position based on contractual re-pricing arrangements at **31 December 2017** is as follows:

	Average effective interest rate	On demand within 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non-interest sensitive	Total
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Banks	N/A	-	-	-	-	383,111	383,111
Due from banks and other money market placements (net)	2.37%	74,081	22,099	-	-	42,490	138,670
Loans, advances and financing activities for customers (net)	5.36%	859,385	600,778	664,225	529,483	-	2,653,871
Financial investments	3.45%	8,955	7,510	54,344	74,247	38,064	183,120
Premises and equipment	N/A	-	-	-	-	65,795	65,795
Other assets	N/A	-	-	-	-	45,785	45,785
Total assets		942,421	630,387	718,569	603,730	575,245	3,470,352
Due to banks and other money market deposits	4.65%	118,390	3,878	-	-	3,489	125,757
Customers' deposits and unrestricted investment accounts	1.64%	315,216	1,100,687	273,338	-	772,026	2,461,267
Euro medium term notes	3.02%	-	-	230,906	-	-	230,906
Other liabilities	N/A	1,782	-	-	-	71,565	73,347
Taxation	N/A	-	-	-	-	7,816	7,816
Tier 1 Perpetual Bond	7.88%	-	-	115,500	-	-	115,500
Subordinated debt	5.09%	-	7,000	18,000	-	-	25,000
Shareholders' equity	N/A	-	-	-	-	430,759	430,759
Total liabilities and shareholders' equity		435,388	1,111,565	637,744	-	1,285,655	3,470,352
Total interest rate sensitivity gap		507,033	(481,178)	80,825	603,730	(710,410)	-
Cumulative interest rate sensitivity gap		507,033	25,855	106,680	710,410	-	

30. RISK MANAGEMENT (Continued)

30.3 Market Risk (Continued)

The bank's interest sensitivity position based on contractual re-pricing arrangements at **31 December 2017** is as follows:

	Average effective interest rate	On demand within 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non-interest sensitive	Total
		USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
Cash and balances with Central Banks	N/A	-	-	-	-	995,094	995,094
Due from banks and other money market placements (net)	2.37%	192,418	57,400	-	-	110,364	360,182
Loans, advances and financing activities for customers (net)	5.36%	2,232,168	1,560,462	1,725,260	1,375,281	-	6,893,171
Financial investments	3.45%	23,260	19,506	141,153	192,849	98,868	475,636
Premises and equipment	N/A	-	-	-	-	170,896	170,896
Other assets	N/A	-	-	-	-	118,922	118,922
Total assets		2,447,846	1,637,368	1,866,413	1,568,130	1,494,144	9,013,901
Due to banks and other money market deposits	4.65%	307,507	10,073	-	-	9,062	326,642
Customers' deposits and unrestricted investment accounts	1.64%	818,743	2,858,927	709,969	-	2,005,262	6,392,901
Euro medium term notes	3.02%	-	-	599,756	-	-	599,756
Other liabilities	N/A	4,629	-	-	-	185,883	190,512
Taxation	N/A	-	-	-	-	20,301	20,301
Tier 1 Perpetual Bond	7.88%	-	-	300,000	-	-	300,000
Subordinated debt	5.09%	-	18,182	46,753	-	-	64,935
Shareholders' equity		-	-	-	-	1,118,854	1,118,854
Total liabilities and shareholders' equity		1,130,879	2,887,182	1,656,478	-	3,339,362	9,013,901
Total interest rate sensitivity gap		1,316,967	(1,249,814)	209,935	1,568,130	(1,845,218)	-
		1,316,967	67,153	277,088	1,845,218	-	

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30. RISK MANAGEMENT (Continued)

30.3 Market Risk (Continued)

The bank's interest sensitivity position based on contractual re-pricing arrangements at 31 December 2016 is as follows:

	Average effective interest rate	On demand within 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non-interest sensitive	Total
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Banks	N/A	253	-	-	-	511,341	511,594
Due from banks and other money market placements (net)	1.29%	55,047	26,181	-	-	34,102	115,330
Loans, advances and financing activities for customers (net)	5.17%	914,600	571,226	647,679	536,776	-	2,670,281
Financial investments	2.28%	8,766	24,633	57,930	5,200	31,854	128,383
Premises and equipment	N/A	-	-	-	-	46,345	46,345
Other assets	N/A	-	-	-	-	60,750	60,750
Total assets		978,666	622,040	705,609	541,976	684,392	3,532,683
Due to banks and other money market deposits	2.46%	110,582	107,281	3,879	-	3,493	225,235
Customers' deposits and unrestricted investment accounts	1.18%	229,266	1,096,042	298,292	-	775,761	2,399,361
Euro medium term notes	2.20%	-	-	233,105	-	-	233,105
Other liabilities	N/A	-	-	-	-	80,062	80,062
Taxation	N/A	-	-	-	-	7,406	7,406
Tier 1 Perpetual Bond	7.88%	-	-	115,500	-	-	115,500
Subordinated debt	5.17%	-	24,100	25,000	-	-	49,100
Shareholders' equity	N/A	-	-	-	-	422,914	422,914
Total liabilities and shareholders' equity		339,848	1,227,423	675,776	-	1,289,636	3,532,683
Total interest rate sensitivity gap		638,818	(605,383)	29,833	541,976	(605,244)	-
Cumulative interest rate sensitivity gap		638,818	33,435	63,268	605,244	-	-

30. RISK MANAGEMENT (Continued)

30.3 Market Risk (Continued)

The bank's interest sensitivity position based on contractual re-pricing arrangements at 31 December 2016 is as follows:

	Average effective interest rate	On demand within 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non-interest sensitive	Total
		USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
Cash and balances with Central Banks	N/A	657	-	-	-	1,328,159	1,328,816
Due from banks and other money market placements (net)	1.29%	142,978	68,003	-	-	88,577	299,558
Loans, advances and financing activities for customers (net)	5.17%	2,375,585	1,483,704	1,682,283	1,394,223	-	6,935,795
Financial investments	2.28%	22,768	63,982	150,468	13,506	82,738	333,462
Premises and equipment	N/A	-	-	-	-	120,377	120,377
Other assets	N/A	-	-	-	-	157,792	157,792
Total assets		2,541,988	1,615,689	1,832,751	1,407,729	1,777,643	9,175,800
Due to banks and other money market deposits	2.46%	287,226	278,652	10,075	-	9,073	585,026
Customers' deposits and unrestricted investment accounts	1.18%	595,497	2,846,862	774,784	-	2,014,964	6,232,107
Euro medium term notes	2.20%	-	-	605,468	-	-	605,468
Other liabilities	N/A	-	-	-	-	207,953	207,953
Taxation	N/A	-	-	-	-	19,236	19,236
Tier 1 Perpetual Bond	7.88%	-	-	300,000	-	-	300,000
Subordinated debt	5.17%	-	62,597	64,935	-	-	127,532
Shareholders' equity	N/A	-	-	-	-	1,098,478	1,098,478
Total liabilities and shareholders' equity		882,723	3,188,111	1,755,262	-	3,349,704	9,175,800
Total interest rate sensitivity gap		1,659,265	(1,572,422)	77,489	1,407,729	(1,572,061)	-
Cumulative interest rate sensitivity gap		1,659,265	86,843	164,332	1,572,061	-	

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The bank has set limits on open positions by currency. Positions are monitored on a daily basis and hedging strategies used to ensure positions are maintained within established limits.

The foreign exchange positions in the books of the bank are generally small residual positions resulting from market coverings for customer transactions.

Foreign exchange VAR is computed monthly for all non-pegged currencies at 99% confidence level and a holding period of 10 days. Additionally earnings impact of a 15% adverse movement in exchange rates for all open positions is factored in the monthly stress tests.

The bank had the following significant net exposures denominated in foreign currencies:

2016	**2017**		**2017**	2016
USD'000	**USD'000**		**RO'000**	RO'000
238,221	**166,571**	US Dollar	**64,130**	91,715
61,031	**78,753**	UAE Dirham	**30,320**	23,497
3,229	**7,369**	Others	**2,837**	1,243

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30. RISK MANAGEMENT (Continued)

30.4 Operational Risk

Operational risk is the risk of loss arising from systems failure, human error, frauds or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The bank cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the bank is able to manage the risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff training and assessment processes, including the use of internal audit. Further, the bank has established an operational loss appetite statement to monitor losses under various operational loss categories and any breaches of set-off thresholds are reported to the Board Risk Committee. In addition to this, the bank has an operational loss reporting database.

Information Security is an essential component of Operational Risk Management. The bank has implemented the latest security infrastructure like firewalls, intrusion prevention systems, anti-virus soft wares, etc. Periodic vulnerability assessments are conducted to ensure the security of the systems.

As a part of Business Continuity Management initiatives, the bank has taken necessary actions to ensure effective measures in case of a crisis situation, e.g. evacuation drills, testing of critical systems and applications from the Disaster Recovery site. The bank has the capability to ensure that critical banking processes are tested to ascertain availability during such situations.

Fraud Risk

The bank has adopted a 'zero tolerance' policy towards fraud and corruption and as such will seek to take disciplinary and/or legal action against those who perpetrate, are involved in, or assist with fraudulent or improper activities. The Fraud risk management (FRM) unit manages the fraud risk for the bank at an enterprise level. The unit monitors transactions originating from Cards, POS and other Digital channels. Besides, the unit conducts Fraud Risk Assessments to assess fraud risks on a pro-active basis, verifies the existing controls and proposes new controls, if required.

The unit is also responsible for managing Incidents across the bank and maintenance of Operational Loss Database.

30.5 Strategic Risks

The bank monitors strategic risks through regular quarterly assessment and reporting at the Board Risk Committee level. This includes reviews of human resource, economic (both at the macro and micro levels), regulatory/compliance, information technology and information security, legal and reputational related risks and the monitoring of strategic project risk arising from initiatives undertaken by the bank. Furthermore, the bank is currently augmenting its Internal Capital Adequacy Assessment Process (ICAAP) to align the business strategy and the capital management processes. In the course of 2017 the bank had engaged an internationally renowned consultant to review the current ICAAP process and to recommend enhancements that will, once implemented, escalate the ICAAP process and documentation to international best practices. This initiative was proposed and sponsored at the highest level by the Board Risk Committee and it will be rolled out in 2018 and progressively completed for the next 2-3 years.

31. CONCENTRATIONS

The bank seeks to manage its credit risk exposure through diversification of lending activities to avoid undue concentrations of risk with individuals or groups of customers in specific locations or businesses. It also obtains security when appropriate.

The distribution of assets, liabilities and contingent items by geographical regions as of **31 December 2017** is as follows:

	Sultanate of Oman	UAE	Egypt	Others	Total
	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Banks	361,419	19,182	2,510	-	383,111
Due from banks and other money market placements (net)	26,357	14,255	1	98,057	138,670
Loans, advances and financing activities for customers (net)	2,537,245	107,724	3	8,899	2,653,871
Financial investments	171,711	9,252	-	2,157	183,120
Premises and equipment	65,096	556	143	-	65,795
Other assets	34,888	10,394	503	-	45,785
Total assets	3,196,716	161,363	3,160	109,113	3,470,352
Due to banks and other money market deposits	508	26,135	13	99,101	125,757
Customers' deposits and unrestricted investment accounts	2,418,602	41,488	1,177	-	2,461,267
Euro medium term notes	230,906	-	-	-	230,906
Other liabilities	67,271	5,764	312	-	73,347
Taxation	6,673	1,032	111	-	7,816
Subordinated debt	25,000	-	-	-	25,000
Shareholders' equity	429,979	(1,213)	1,993	-	430,759
Tier 1 perpetual bond	115,500	-	-	-	115,500
Liabilities and shareholders' equity	3,294,439	73,206	3,606	99,101	3,470,352
Contingent liabilities	396,486	26,304	10	24,307	447,107

31. CONCENTRATIONS (Continued)

	Sultanate of Oman	UAE	Egypt	Others	Total
	USD'000	USD'000	USD'000	USD'000	USD'000
Cash and balances with Central Banks	938,752	49,823	6,519	-	995,094
Due from banks and other money market placements (net)	68,460	37,026	3	254,693	360,182
Loans, advances and financing activities for customers (net)	6,590,246	279,803	8	23,114	6,893,171
Financial investments	446,002	24,031	-	5,603	475,636
Premises and equipment	169,081	1,444	371	-	170,896
Other assets	90,618	26,998	1,306	-	118,922
Total assets	8,303,159	419,125	8,207	283,410	9,013,901
Due to banks and other money market deposits	1,319	67,883	34	257,406	326,642
Customers' deposits and unrestricted investment accounts	6,282,083	107,761	3,057	-	6,392,901
Euro medium term notes	599,756	-	-	-	599,756
Other liabilities	174,731	14,971	810	-	190,512
Taxation	17,332	2,681	288	-	20,301
Subordinated debt	64,935	-	-	-	64,935
Shareholders' equity	1,116,828	(3,151)	5,177	-	1,118,854
Tier 1 perpetual bond	300,000	-	-	-	300,000
Liabilities and shareholders' equity	8,556,984	190,145	9,366	257,406	9,013,901
Contingent liabilities	1,029,834	68,322	26	63,135	1,161,317

The distribution of assets, liabilities and off balance sheet items by geographical regions as of 31 December 2016 is as follows:

	Sultanate of Oman	UAE	Egypt	Others	Total
	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Banks	483,349	25,716	2,529	-	511,594
Due from banks and other money market placements (net)	15,400	10,816	116	88,998	115,330
Loans, advances and financing activities for customers (net)	2,433,983	203,248	3	33,047	2,670,281
Financial investments	114,508	11,100	-	2,775	128,383
Premises and equipment	45,720	486	139	-	46,345
Other assets	48,987	11,323	440	-	60,750
Total assets	3,141,947	262,689	3,227	124,820	3,532,683
Due to banks and other money market deposits	756	36,583	2,695	185,201	225,235
Customers' deposits and unrestricted investment accounts	2,303,115	95,080	1,166	-	2,399,361
Euro medium term notes	233,105	-	-	-	233,105
Other liabilities	68,358	11,413	291	-	80,062
Taxation	7,113	189	104	-	7,406
Subordinated debt	49,100	-	-	-	49,100
Shareholders' equity	415,113	6,033	1,768	-	422,914
Tier 1 perpetual bond	115,500	-	-	-	115,500
Liabilities and shareholders' equity	3,192,160	149,298	6,024	185,201	3,532,683
Contingent liabilities	446,421	35,208	2,890	59,179	543,698

31. CONCENTRATIONS (Continued)

The distribution of assets, liabilities and off balance sheet items by geographical regions as of 31 December 2016 is as follows:

	Sultanate of Oman USD'000	UAE USD'000	Egypt USD'000	Others USD'000	Total USD'000
Cash and balances with Central Banks	1,255,452	66,795	6,569	-	1,328,816
Due from banks and other money market placements (net)	40,000	28,094	301	231,163	299,558
Loans, advances and financing activities for customers (net)	6,322,034	527,917	8	85,836	6,935,795
Financial investments	297,423	28,831	-	7,208	333,462
Premises and equipment	118,754	1,262	361	-	120,377
Other assets	127,239	29,410	1,143	-	157,792
Total assets	8,160,902	682,309	8,382	324,207	9,175,800
Due to banks and other money market deposits	1,964	95,021	7,000	481,041	585,026
Customers' deposits and unrestricted investment accounts	5,982,117	246,961	3,029	-	6,232,107
Euro medium term notes	605,468	-	-	-	605,468
Other liabilities	177,553	29,644	756	-	207,953
Taxation	18,475	491	270	-	19,236
Subordinated debt	127,532	-	-	-	127,532
Shareholders' equity	1,078,216	15,670	4,592	-	1,098,478
Tier 1 perpetual bond	300,000	-	-	-	300,000
Liabilities and shareholders' equity	8,291,325	387,787	15,647	481,041	9,175,800
Contingent liabilities	1,159,535	91,449	7,506	153,712	1,412,202

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32. SEGMENTAL INFORMATION

For management purposes, the bank is organised into four operating segments based on business units and are as follows:

- Retail banking offers various products and facilities to individual retail and high networth customers to meet everyday banking needs. This includes asset products like personal loans, housing loan, credit cards and term loans and liability products like savings account, current account and term deposits.
- Wholesale banking delivers a variety of products and services to corporate customers that include lending, accepting deposits, trade finance, treasury and foreign exchange. It also includes investment banking which offers investment products such as asset management, corporate advisory and brokerage services to retail customers and institutional clients.
- Commercial banking covers the mid-tier corporate and SME customers offering the entire spectrum of products to suit their business needs. It also includes international operations of UAE and Egypt and Islamic banking which offers products as per Sharia principles.
- Funding Center – The Funding center is responsible for balancing and managing the liquidity of funds within the bank. It acts as repository of funds by allocating funds transfer pricing to various business units for performance management purposes. The department also handles the bank's investments in securities, asset/liability management and cash instruments.

Management monitors the operating results of these segments separately for the purpose of making decisions about resource allocation and performance assessment. The costs incurred by the central functions are managed on a group basis and are not allocated to operating segments.

Segment information by business line is as follows:

Year ended 31 December 2017	Retail banking RO'000	Wholesale banking RO'000	Commercial banking RO'000	Funding center RO'000	Total RO'000
Net Interest income and Income from Islamic financing and Investment activities	42,427	27,146	15,165	8,192	92,930
Other income	13,837	18,116	4,194	3,052	39,199
Operating profit	18,098	33,392	4,897	11,224	67,611
Impairment provisions (net) and taxation	(2,542)	426	(11,819)	(9,650)	(23,585)
Profit/(loss)	15,556	33,818	(6,922)	1,574	44,026
Total assets	1,256,293	1,152,082	449,745	612,232	3,470,352
Total liabilities and equity	814,830	1,369,017	426,059	860,446	3,470,352

Year ended 31 December 2017	Retail banking USD'000	Wholesale banking USD'000	Commercial banking USD'000	Funding Center USD'000	Total USD'000
Net Interest income and Income from Islamic financing and Investment activities	110,200	70,509	39,390	21,278	241,377
Other income	35,940	47,055	10,894	7,927	101,816
Operating profit	47,008	86,732	12,721	29,153	175,614
Impairment provisions (net) and taxation	(6,603)	1,106	(30,699)	(25,065)	(61,261)
Net Profit	40,405	87,838	(17,978)	4,088	114,353
Total assets	3,263,099	2,992,420	1,168,168	1,590,214	9,013,901
Total liabilities and equity	2,116,441	3,555,889	1,106,646	2,234,925	9,013,901

32. SEGMENTAL INFORMATION (Continued)

For management purposes the bank also reports the segment information of its operations by the following geographical locations:

i. Oman

ii. United Arab Emirates (UAE)

iii. Egypt

Transactions between the above segments are conducted at estimated market rates on an arm's length basis.

Segment information by geography is as follows:

Year ended 31 December 2017	Oman RO'000	UAE RO'000	Egypt RO'000	Total RO'000
Interest income and Income from Islamic financing and Investment activities	141,827	8,138	422	150,387
Other operating income	37,568	1,623	8	39,199
Total income	179,395	9,761	430	189,586
Interest costs and Unrestricted investment				
account holders' share of profit	54,870	2,531	56	57,457
Other operating expenses	55,466	4,624	216	60,306
Depreciation	4,080	132	-	4,212
Credit loss expense - customer loan	11,141	13,972	-	25,113
Recoveries	(7,798)	(1,604)	(75)	(9,477)
Impairment losses on available-for-sale investments	688	-	-	688
Credit loss write back – bank loans	26	-	-	26
Taxation	9,962	(2,736)	9	7,235
Total	128,435	16,919	206	145,560
Segment profit for the year	50,960	(7,158)	224	44,026
Other information				
Segment assets	3,296,610	153,732	20,010	3,470,352
Segment capital expenses	23,479	201	-	23,680

32. SEGMENTAL INFORMATION (Continued)

Year ended 31 December 2017	Oman USD'000	UAE USD'000	Egypt USD'000	Total USD'000
Interest income and Income from Islamic financing and Investment activities	368,382	21,138	1,096	390,616
Other operating income	97,579	4,216	21	101,816
Total income	465,961	25,354	1,117	492,432
Interest costs and Unrestricted investment account holders' share of profit	142,519	6,575	145	149,239
Other operating expenses	144,068	12,010	561	156,639
Depreciation	10,597	343	-	10,940
Credit loss expense - customer loan	28,938	36,291	-	65,229
Recoveries	(20,254)	(4,166)	(195)	(24,615)
Impairment losses on available-for-sale Investments	1,787	-	-	1,787
Credit loss write back – bank loans	68	-	-	68
Taxation	25,875	(7,106)	23	18,792
Total	333,598	43,947	534	378,079
Segment profit for the year	132,363	(18,593)	583	114,353
Other information				
Segment assets	8,562,623	399,304	51,974	9,013,901
Segment capital expenses	60,984	522	-	61,506

Segment information by business line is as follows:

Year ended 31 December 2016	Retail banking RO'000	Wholesale banking RO'000	Commercial banking RO'000	Funding center RO'000	Total RO'000
Net income	40,814	28,188	18,098	14,465	101,565
Other income	13,405	14,516	4,575	2,052	34,548
Operating profit	17,809	30,898	8,503	16,240	73,449
Impairment provisions (net) and taxation	(3,038)	3,443	(10,816)	(7,259)	(17,670)
Profit/(loss)	14,771	34,341	(2,313)	8,980	55,779
Total assets	1,236,289	1,093,872	558,233	644,288	3,532,683
Total liabilities and equity	817,441	1,275,681	527,563	911,998	3,532,683

32. SEGMENTAL INFORMATION (Continued)

Year ended 31 December 2016	Retail banking USD'000	Wholesale banking USD'000	Commercial banking USD'000	Funding center USD'000	Total USD'000
Net income	106,010	73,216	47,008	37,571	263,805
Other income	34,818	37,704	11,883	5,330	89,735
Operating profit	46,257	80,253	22,085	42,181	190,776
Impairment provisions (net) and taxation	(7,891)	8,944	(28,093)	(18,856)	(45,896)
Profit/(loss)	38,366	89,197	(6,008)	23,325	144,880
Total assets	3,211,142	2,841,226	1,449,956	1,673,476	9,175,800
Total liabilities and equity	2,123,223	3,313,457	1,370,294	2,368,826	9,175,800

Segment information by geography is as follows:

For the year ended 31 December 2016	Oman RO'000	UAE RO'000	Egypt RO'000	Total RO'000
Interest income and Income from Islamic financing and Investment activities	130,683	10,400	369	141,452
Other operating income	31,827	2,731	(10)	34,548
Total income	162,510	13,131	359	176,000
Interest costs and Unrestricted investment account holders' share of profit	37,246	2,576	65	39,887
Other operating expenses	55,495	3,946	359	59,800
Depreciation	2,748	116		2,864
Credit loss expense - customer loan	9,594	10,051	1	19,646
Recoveries	(9,035)	(685)	(40)	(9,760)
Impairment losses on available-for-sale investments	210	-	-	210
Credit loss expense – bank loans	(62)	-	-	(62)
Taxation	7,431	187	18	7,636
Total	1,03,627	16,191	403	120,221
Segment profit for the year	58,883	(3,060)	(44)	55,779
Other information				
Segment assets	3,250,952	2,61,964	19,767	3,532,683
Segment capital expenses	14,469	303	-	14,772

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32. SEGMENTAL INFORMATION (Continued)

For the year ended 31 December 2016	Oman USD'000	UAE USD'000	Egypt USD'000	Total USD'000
Interest income and income from Islamic financing and Investment activities	339,436	27,013	958	367,408
Other operating income	82,668	7,094	(26)	89,735
Total Income	422,104	34,107	932	457,143
Interest costs and Unrestricted investment account holders' share of profit	96,743	6,691	169	103,603
Other operating expenses	144,143	10,250	932	155,325
Depreciation	7,138	301	-	7,439
Credit loss expense - customer loan	24,919	26,106	4	51,029
Recoveries	(23,468)	(1,779)	(104)	(25,351)
Impairment losses on available-for-sale Investments	545	-	-	545
Credit loss expense – bank loans	(161)	-	-	(161)
Taxation	19,301	486	47	19,834
Total	269,160	42,055	1,048	312,263
Segment profit for the year	152,944	(7,948)	(116)	144,880
Other information				
Segment assets	8,444,031	680,426	51,343	9,175,800
Segment capital expenses	37,582	787	-	38,369

33. FAIR VALUE OF FINANCIAL INSTRUMENTS

Based on the valuation methodology outlined below, the fair values of all financial instruments at 31 December 2017 are considered by the Management not to be materially different to their book values.

Estimation of fair values

The following summarises the major methods and assumptions used in estimating the fair values of assets and liabilities:

Loans and advances

Fair value is calculated based on discounted expected future principal and interest cash flows. Loan repayments are assumed to occur at contractual repayment dates, where applicable. For loans that do not have fixed repayment dates or that are subject to prepayment risk, repayments are estimated based on experience in previous periods when interest rates were at levels similar to current levels, adjusted for any differences in interest rate outlook. Expected future cash flows are estimated considering credit risk and any indication of impairment. Expected future cash flows for homogeneous categories of loans are estimated on a portfolio basis and discounted at current rates offered for similar loans to new borrowers with similar credit profiles. The estimated fair values of loans reflect changes in credit status since the loans were made and changes in interest rates in the case of fixed rate loans.

Investments

Fair value is based on quoted market prices at the reporting date without any deduction for transaction costs. If a quoted market price is not available, fair value is estimated based on discounted cash flow and other valuation techniques.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market-related rate for a similar instrument at the reporting date.

Current account balances due to and due from banks

The carrying amount of current account balances due to and from banks was considered to be a reasonable estimate of fair value due to their short term nature.

Bank and customer deposits

For demand deposits and deposits with no defined maturities, fair value is taken to be the amount payable on demand at the reporting date. The estimated fair value of fixed-maturity deposits, including certificates of deposit, is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities. The value of long-term relationships with depositors is not taken into account in estimating fair values.

Other financial instruments

No fair value adjustment is made with respect to credit-related off-balance sheet financial instruments, which include commitments to extend credit, standby letters of credit and guarantees, as the related future income streams materially reflect contractual fees and commissions actually charged at the reporting date for agreements of similar credit standing and maturity.

Foreign exchange contracts are valued based on market prices. The market value adjustments in respect of foreign exchange contracts are included in other assets and other liabilities.

The fair values of financial instruments that are traded in active markets are based on quoted market prices or dealer price quotations. Other unquoted equities are valued based on information provided by fund managers, investee financial information and current purchase prices.

The bank measures fair values using the following fair value hierarchy, which reflects the significance of the inputs used in making the measurements.

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33. FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

Valuation models

Level 1: inputs that are quoted market prices (unadjusted) in active markets for identical instruments.

Level 2: inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.

Level 3: inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The following table shows an analysis of financial instruments other than derivatives instruments recorded at fair value by level of the fair value hierarchy:

Total USD'000	Level 2 USD'000	Level 1 USD'000	31 December 2017	Level 1 RO'000	Level 2 RO'000	Total RO'000
			Investments – held for trading :			
143,431	-	143,431	Government development bonds	55,221	-	55,221
1,429	-	1,429	Quoted bond	550	-	550
144,860	-	144,860	Total	55,771	-	55,771
			Investments - available-for-sale:			
10,117	-	10,117	Government development bonds	3,895	-	3,895
67,210	-	67,210	Quoted equities	25,876	-	25,876
20,231	20,231	-	Other unquoted equities	-	7,789	7,789
97,558	20,231	77,327	Total	29,771	7,789	37,560
242,418	20,231	222,187	Total financial assets	85,542	7,789	93,331

Total USD'000	Level 2 USD'000	Level 1 USD'000	31 December 2016	Level 1 RO'000	Level 2 RO'000	Total RO'000
			Investments – held for trading:			
168,156	-	168,156	Government development bonds	64,740		64,740
2,358	-	2,358	Quoted equities	908	-	908
170,514	-	170,514	Total Investments - available-for-sale:	65,648	-	65,648
48,719		48,719	Quoted equities	18,757	-	18,757
31,660	31,660	-	Other unquoted equities	-	12,189	12,189
80,379	31,660	48,719	Total	18,757	12,189	30,946
250,893	31,660	219,233	Total financial assets	84,405	12,189	96,594

The bank's primary medium and long-term financial liabilities are the borrowed funds and subordinated liabilities. The fair values of these financial liabilities not materially different from their carrying values, since these liabilities are repriced at intervals of three or six months, depending on the terms and conditions of the instrument and the resultant applicable margins approximate the current spreads that would apply for borrowings with similar maturities

Derivative financial instrument at level 2 are valued based on counter party valuation, quoted forward rates and yield curves (see note 34).

34.DERIVATIVES

In the ordinary course of business the bank enters into various types of transactions with customers and for own account for hedging purpose that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instrument, reference rate or index. The bank uses the following derivative financial instruments:

Derivative product types

Forwards are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market.

Swaps are contractual agreements between two parties to exchange movements in interest or foreign currency rates and equity indices, and (in the case of credit default swaps) to make payments with respect to defined credit events based on specified notional amounts.

Options are contractual agreements that convey the right, but not the obligation, to either buy or sell a specific amount of a commodity, foreign currency or financial instrument at a fixed price, either at a fixed future date or at any time within a specified period.

Derivatives held or issued for hedging purposes

As part of its asset and liability management the bank uses derivatives for hedging purposes in order to reduce its exposure to currency and interest rate risks. Hedging specific financial instruments and forecasted transactions as well as strategic hedging against overall balance sheet exposures achieve this.

The bank uses forward foreign exchange contracts, options and currency swaps to hedge against specifically identified currency risks. In addition, the bank uses interest rate swaps to hedge against the cash flow risks arising from certain fixed interest rate loans and deposits.

For interest rate risk strategic hedging is carried out by monitoring the re-pricing of financial assets and liabilities and entering into interest rate swaps to hedge a proportion of the interest rate exposure.

The bank has entered into an interest rate swap, which is designated as a fair value hedge, for hedging the interest rate risk on Euro medium term notes. The cumulative change in the fair value of the Euro medium term notes (hedged item) attributable to the risk hedged is recorded as part of the carrying value of the Euro medium term notes and accordingly presented in statement of financial position.

The table below shows the positive and negative fair values of derivative financial instruments entered with and on behalf of customers, which are equivalent to the market values, together with the notional amounts analysed by the term to maturity. The notional amount is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured.

34. DERIVATIVES (Continued)

31 December 2017	Positive fair value RO'000 (9 note)	Negative fair value RO'000 (13 note)	Notional amount RO'000	Notional amounts by term to maturity		
				Within 3 months RO'000	3 - 12 months RO'000	1 - 5 years RO'000
Fair value hedge	-	(94)	192,500	-	-	192,500
Interest rate swaps	1,842	(1,842)	95,238	6,285	13,971	74,982
Forward foreign exchange purchase contracts	508	(122)	212,849	175,508	13,879	23,462
Forward foreign exchange sales contracts	345	(910)	212,849	168,623	20,710	23,516
Currency options	6	(6)	13,193	8,579	4,614	-
Total	2,701	(2,974)	726,629	358,995	53,174	314,460
Total – USD'000	7,016	(7,725)	1,887,348	932,455	138,114	816,779

31 December 2016	Positive fair value RO'000 (note 9)	Negative fair value RO'000 (note 13)	Notional amount RO'000	Notional amounts by term to maturity		
				Within 3 months RO'000	3 - 12 months RO'000 -	1 - 5 years RO'000
Fair value hedge	2,105	-	192,500	-	-	192,500
Interest rate swaps	2,981	(2,981)	112,152	2,660	14,484	95,008
Forward purchase contracts	821	(2)	187,531	173,133	14,398	-
Forward sales contracts	2,432	(2,593)	187,531	174,155	13,376	-
Currency options	58	(58)	2,835	2,159	676	-
Total	8,397	(5,634)	682,549	352,107	42,934	287,508
Total – USD'000	21,810	(14,634)	1,772,855	914,564	111,517	746,774

35.COMPARATIVE AMOUNTS

Certain of the corresponding figures for 2016 have been reclassified in order to conform with the presentation for the current year. Such reclassifications are not considered material and made within the same notes to the financial statements and do not affect previously reported profit or equity.

Muzn Islamic Banking

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C.R. No. 1224013
PR No. HMH/15/2015; HMA/9/2015

REPORT ON FACTUAL FINDINGS TO THE BOARD OF DIRECTORS OF NATIONAL BANK OF OMAN SAOG IN RESPECT OF BASEL II - PILLAR III AND BASEL III RELATED DISCLOSURES

We have performed the procedures agreed with you and as prescribed in the Central Bank of Oman's (CBO) circular No. BM 1027 dated 4 December 2007 with respect to the Basel II - Pillar III Disclosures and Basel III related Disclosures (the disclosures) of National Bank of Oman SAOG ("the bank") as at and for the year ended 31 December 2017. The disclosures were prepared by the management in accordance with the CBO's Circular No. BM 1009 dated 13 September 2006, Circular No. BM 1027 dated 4 December 2007 and Circular number 1114 dated 17 November 2013. Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon procedures engagements. The procedures, as set out in Circular No. BM 1027, were performed solely to assist you in evaluating the bank's compliance with the related disclosure requirements set out in CBO Circular No. BM 1009 dated 13 September 2006 and BM 1114 dated 17 November 2013.

We report our findings as follows:

Based on performance of the procedures detailed above, we found the disclosures free from any material misrepresentation.

Because the above procedures do not constitute either an audit or a review made in accordance with International Standards on Auditing or International Standards on Review Engagements, we do not express any assurance on the disclosures.

Had we performed additional procedures or had we performed an audit or review of the disclosures in accordance with the International Standards on Auditing or International Standards on Review Engagements, other matters might have come to our attention that would have been reported to you.

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose. This report relates only to the accompanying disclosures to be included in the bank's annual report for the year ended 31 December 2017 and does not extend to any financial statements of the bank taken as a whole or to any other reports of the bank.

Ernst & Young LLC

Muscat
10 March 2018

ارنست ويونغ ش م م
س ت: ١٢٢٤٠١٣
ص ب: ١٧٥٠ روي - ١١٢، سلطنة عمان
EY ERNST & YOUNG LLC
C.R. No. 1224013
P.O. Box 1750 - P.C. 112, Sultanate of Oman

December 31, 2017
Report of Shari'a Supervisory Board
Muzn Islamic Banking Services
National Bank of Oman,
Oman.

مزن للصيرفة الإسلامية
Muzn Islamic Banking

In the name of Allah, the Beneficent, The Merciful

To the Shareholders of Muzn Islamic Banking Services

Assalam Alaikum Wa Rahmat Allah Wa Barakatuh

In compliance with the Letter of appointment, we are required to submit the following report:

We have reviewed the principles and the contracts relating to the transactions and applications introduced by the Muzn Islamic Banking Services during the period ended. We have also conducted our review to form an opinion as to whether the Muzn Islamic Banking Services complied with Shari principles and also with the specific Fatawa, rulings and guidelines issued by us.

We conducted our review which included examining, on a test basis, of each type of transactions, the relevant documentation and procedures adopted by the Muzn Islamic Banking Services.

We planned and performed our review so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Muzn Islamic Banking Services has not violated Shari'a principles. In our opinion:

a) The Contracts, transactions, and dealings entered into by the Muzn Islamic Banking Services during the year ended 31st December 2017 that we have reviewed are in compliance with Shari'a principles.

b) The allocation of profit & charging of losses relating to investment account conform to the basis that had been approved by us in accordance with Shari'a principles.

c) Earnings that have been realized from sources or by means prohibited by Shari'a principle have been identified and segregated for disposal to charity.
d) Calculation and payment of Zakah is the individual responsibility of Shareholders and Depositors.

We beg Allah the Almighty to grant us all the success and straight forwardness.

Wassalam Alaikum Wa Rahmat Allah Wa Barakatuh

Sheikh Dr. Mohamed Bin Ali Elgari
Chairman Shari'a Supervisory Board

Sheikh Dr. Mohammed Daud Bakar
Muzn Shari'a Supervisory Board Member

Sheikh Saleh Bin Nasser Al Kharusi
Muzn Shari'a Supervisory Board Member

HH Dr. Adham Bin Turki Al Said
Muzn Non-Voting SSB Member

Dr. Khalid Bin Said Al Aamri
Muzn Non-voting SSB Member

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As per requirement of IBRF Title2, Clause No. 2.2.2.14

Shari'a rulings along with their bases:

Reference No.	Fatwa Title	Detail
01/2017	Sale and Lease Back under Diminishing Musharaka Mode	There is no juristic evidence prohibiting use of Sale and lease back mode under Diminishing Musharaka. As per AAOIFI Shari'a Standard No (9), Article No. 3/6, "An institution's customer may jointly acquire assets that he wishes to lease with the institution, and then lease the institution's share of the asset from the institution. In the case, the rental specified as receivable by the institution should only be in a proportion to its share in the ownership of the asset, since the lessee is a co-owner of the asset and therefore has to pay rent only on the share that does not own."
02/2017	Wakalah Bil-Istithmar	The juristic base of this Product is on the concept of Wakalah Bil-Istithmar. Under this concept, Bank becomes the Principal (Muwakkil) and Customer becomes the Wakeel (Agent) of the funds. These funds are invested in Shari'a compliant business to generate and distribute profits according to Wakalah contract. The concept has already been approved by AAOIFI.
03/2017	Islamic Personal Financing – Consumer Services Ijarah	Islamic Personal Financing – Consumer Services Ijarah is based on the concept of Ijarah which is based on the religious evidence of the Qur'an, Sunnah and the consensus of the jurists. On the level of Qur'an Allah Almighty says: "One of the women said, "O my father, hire him. Indeed, the best one you can hire is the strong and the trustworthy"(1), and "If you had wished, surely, you could have taken wages for it!" (2) .The authority of permissibility of Ijarah in the Sunnah is saying of the prophet (peace be upon him): "whoever hired a worker must inform him of his wages" (3). The juristic base of this Product is based on the concept of Ijarah. Under this concept, Bank becomes (Lessor) after acquiring the service from service provider (vendor), and leases it to the Customer who becomes the lessee of the services.

(1) [Surah Al Qasas (The Narrative): verse 26]
(2) [Surah Al Kahf, verse 77]
(3) This hadith has been related by Ibn Majah in his "Sunan" [2:817]; and Al-Haythami in his "Majam' Al-Zawa'id" [4:98]

Introduction

MUZN ISLAMIC BANKING– WINDOW OF NATIONAL BANK OF OMAN SAOG, was established in the Sultanate of Oman to carry out banking and other financial activities in accordance with Islamic Sharia rules and regulations. Muzn operates under an Islamic Banking license granted by the Central Bank of Oman on 17 January 2013. Muzn's Sharia Supervisory Board is entrusted to ensure adherence to Sharia rules and principles in its transactions and activities. A complete set of financial statements of Muzn is included in the consolidated financial statements of the bank. This document presents Basel II, Pillar III disclosure pertaining to Muzn on a standalone basis. There is no restriction on the transfer of the funds from the bank towards Muzn. However under the Islamic Banking regulatory framework (IBRF), Muzn cannot place funds with the bank. Muzn does not hold controlling interest in any other entity.

CAPITAL STRUCTURE

The assigned capital of the MUZN ISLAMIC BANKING as at 31 December 2017 is 13,500,000. Muzn' s capital structure as at close of 31 December 2017, based on Central Bank of Oman's (CBO) guidelines is as follows:

Elements of Capital	Amount in RO 000's
Tier I Capital **Local Banks**	
Paid-up capital	13,500
Share premium	-
Legal reserve	-
General reserve	-
Subordinated debt reserve	-
Stock dividend(Proposed)	-
Retained earnings/loss*	(2,409)
Common equity Tier 1 before regulatory adjustments	**11,091**
Deduction	
Deferred tax asset	-
Common equity Tier 1	**11,091**
Tier I capital after all deductions	**11,091**
Tier II Capital	
Revaluation reserves / Cumulative fair value gains or losses on available for sale instruments	-
General loan loss provision/General loan loss reserve	913
Subordinated debt (After amortization)	-
Total Tier II Capital	913
Total Regulatory Capital	12,004
Amount of investment account holders funds	114,108
Profit equalization reserve	254
Investment risk reserve	93
TOTAL INVESTMENT OF ACCOUNT HOLDERS	**114,456**

Basel II and III - Pillar III Report 2017

CAPITAL ADEQUACY

Qualitative Disclosures:

The ultimate objectives of capital management are three fold:

- Ensure stability of the Islamic window by holding enough capital to cover unexpected loss
- Enhance the efficiency of the Bank, by increasing the risk adjusted return at various levels of aggregation (and thereby ensuring that "excess" capital is not held unnecessarily).
- Incentivize informed decision making and proactive risk management through an efficient and effective allocation of capital across the business.

The capital management plan envisaged for Muzn is based on the regulatory risk capital framework of Basel II and uses the standardized approach for calculating the credit as well market risk, and the basic indicator approach for operational risk as prescribed by CBO.

The capital management policy is aligned to the policy of the Bank, and aims to ensure that on a risk adjusted return on capital basis (RAROC) Muzn is allocated an appropriate amount of capital. The RAROC model has been implemented for the entire portfolio except for Retail banking where the Central Bank of Oman has defined caps on profit rates, which are followed.

The Asset Liability Committee (ALCO) currently reviews and monitors capital adequacy and requirement for capital on an ongoing basis both for the Muzn window and its divisions that require capital to be assigned separately. Risk weights are assigned to assets as per regulatory requirements from CBO. Assets funded by investment accounts are also assigned same risk weights as assets funded by own equity.

Qualitative Disclosures:

A set of triggers is followed as part of the capital management so as to provide the bank with an early warning system in terms of its level of capital, and to enable it to take suitable measures at an early stage to prevent capital falling below acceptable limits. For this purpose it has been decided by ALCO that the triggers set for the Bank will become applicable for Muzn as well.

The Bank prepares ICAAP (Internal Capital Adequacy Assessment Process) document in line with Basel II guidelines to evaluate all Enterprise-wide Risks that are not fully captured in the Pillar I Risks. Following the guidelines issued by the Central Bank of Oman in December 2012, assessment under ICAAP comprehensively for the whole bank is carried out and submitted to the Central Bank of Oman in accordance with the prescribed guidelines. The bank will also factor in the regulatory guidelines, wherever applicable on Basel III, while carrying out its assessment. Currently, a separate ICAAP is not prepared for Muzn.

Quantitative Disclosures:

Position as at 31.12.2017 (RO'000)

Details	Amount in RO 000's
Tier I capital (after supervisory deductions)	**11,091**
Tier II capital (after supervisory deductions & up to eligible limits)	**913**
Risk Weighted Assets (RWAs) – Banking Book	**73,071**
Risk Weighted Assets (RWAs) – Operational Risk	**4,572**
Total Risk Weighted Assets (RWAs) – Banking Book + Operational Risk	**77,643**
Minimum required capital to support RWAs of banking book and operational risk	10,288
Minimum required capital comprises of;	
i) Tier I capital	9,374
ii) Tier II capital	913
Balance Tier I capital available for supporting Trading Book	1,717
Balance Tier II capital available for supporting Trading book	-
Risk Weighted Assets (RWAs) – Trading Book	**2.6**
Total capital required to support Trading Book	0.3
Minimum Tier I capital required for supporting Trading Book	0.1
Total Regulatory Capital	**12,004**
Total Risk Weighted Assets – Islamic Window	**77,646**
BIS Capital Adequacy Ratio	**15.5**

Basel II and III - Pillar III Report 2017

Basel III Disclosures:

In compliance with CBO circular BM 1114 dated 17 November 2013; mandatory disclosures are made in this report.

Certain additional capital adequacy disclosures are as follows:

Position as at 31.12.2017 (RO'000)

Details	Gross balance (Book value)	Net balance (Book value)	Risk Weighted Assets
On balance sheet items	135,637	134,304	71,974
Off balance sheet items	1447	1447	1,097
Derivatives	-	-	-
Operational Risk	-	-	4,572
Market Risk	-	-	3
Total	137,084	135,751	77,646
Common equity Tier I Capital	-	-	-
Additional Tier 1 Capital	-	-	-
Tier 2 Capital	-	-	-
Total Regulatory Capital	12,004	-	-
Total required Capital @13.25%	10,288	-	-
Capital requirement for credit risk	9,682	-	-
Capital requirement for market risk	-	-	-
Capital requirement for operational risk	606	-	-
Common equity Tier 1 Ratio	14.28	-	-
Tier I Ratio	14.28	-	-
Total Capital ratio	15.46	-	-

Disclosures for Investment Account Holders (IAH)

Muzn accepts funds from investment account holders (IAH) under Sharia compliant Mudaraba contracts and Wakala agreements. These funds are unrestricted in nature i.e. it is at the discretion of Muzn to invest in any Sharia compliant assets. There are no limits on the investment of IAH fund in any particular type of asset.

Currently, Muzn offers three types of Investment accounts:

- Savings accounts,
- Term deposits of various maturities from 1 month to five years and
- Flex Wakala

Investment from investment account holders (IAH) is pooled with Muzn's funds. Mudarib (Manager of assets) expenses are charged to a pool which includes all direct expenses incurred, including impairment provisions. Fee based income is not allocated to the joint pool. From the distributable profits earned by the pool assets, and after charging Mudarib expenses, allocation is made between shareholder funds and funds of IAH.

Under Wakala arrangement for Islamic Wakala Investment, the customer becomes the Principal (Muwakkil), and Muzn becomes the Investment Agent (Wakeel) for the funds invested by the customer. Muzn will accept deposits from Wakala Investment holders under a Wakala agreement and allocate these funds to an investment pool. While accepting the deposit from the customers, Bank informs the "Expected Targeted Profit Rate" on the deposit. Funds from this investment pool will be utilized to provide financing to customers under Islamic modes and to invest in other Sharia compliant investments opportunities. The profit earned from the investment and financing activities from the investment pool, shall be paid to the investors (as the Muwakkil) based on their pre-assigned weightages less performance fee and the fixed fees payable to the bank (as a Wakeel). Investor's share of profit shall be returned to the investors together with the principal on maturity date.

Muzn appropriates an amount in excess of the profit to be distributed to investment account holders before taking into consideration the Mudarib (Manager of assets) share of income. This reserve is called Profit Equalization Reserve (PER). Further, Investment Risk Reserve (IRR) is also maintained out of the income of investment account holders, after allocating the mudarib share, in order to cater against future losses for investment account holders.

Ratios and returns

Profit Equalization Reserve (PER) to Profit Sharing Investment Account(PSIA)

Particulars (RO'000)	2017	2016
Amount of Total PER	254	198
Amount of PSIA by IAH	114,108	118,117
PER to PSIA Ratio	0.22%	0.17%
Investment Risk Reserves Reserve (PER) to Profit Sharing Investment Account(PSIA)		
Amount of Total IRR	93	68
Amount of PSIA by IAH	114,108	118,117
IRR to PSIA Ratio	0.08%	0.06%
Return on Assets (ROA)		
Amount of total net income (before distribution of profit to unrestricted IAH)	5,013	4,070
Amount of assets	114,108	136,578
Return on assets (ROA)	3.73%	2.98%
Return on Equity (ROE)		
Amount of total net income (after distribution of profit to unrestricted IAH)	1,871	2,498
Amount of equity	11,091	11,148
Return on equity (ROE)	16.87%	22.40%

Rate of profit distributed to PSIA by type of IAH

As at reporting date, Muzn has only unrestricted IAH and has distributed profit amounting RO 3,061,000 during the year.

Latest Profit rates paid to investment account holders for quarter ended 31 December 2017

	Weightages	Declared Profit Rate
Savings Account (Mudarabah)	20	%0.70
Flexi Wakala	40	%0.10
Flexi Wakala - Elite	50	2.25%
Flexi Wakala - Premium	25	1.75%
Wakala- Upto 6 months	30	0.10% - 0.25%
Wakala - > 6months to 1 Year	50	0.40% - 0.75%
Wakala - > 1 Year to 3 Years	80	1.75% - 2.50%
Wakala - > 3 Years	100	3.00% - 3.50%
Government Flexi Wakala	50	%1.00

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Jointly Funded Assets and Return to IAH

	31 December 2017	31 December 2016
Assets		
Deferred sale under Murabah	**1,665**	1,730
Ijara Muntahia Bittamleek	**85,452**	84,061
Diminishing Musharaka	**11,008**	12,082
Forward Ijara	**4,656**	7,226
Total amount invested	**102,781**	105,099
Share of profit of IAH before PER and IRR for the year	**3,142**	1,572
Transfers to:		
PER	**(56)**	(25)
IRR	**(25)**	(11)
Share of profit of IAH after PER and IRR for the year	**3,061**	1,536

RISK EXPOSURE AND ASSESSMENT:

Risk Management

The primary objective of risk management is to appropriately safeguard the Bank's resources from the various risks which the Bank faces. Muzn's risk management incorporates the same essential principles and practices that govern the Bank's risk management which are detailed in the Bank's Basel II disclosures.

Bank's risk management processes have proven effective for Muzn throughout the current year. The bank's Board of Directors has remained closely involved with key risk management initiatives, and ensured that Muzn's risks are effectively managed and adequate capital is held in line with the requirements. Detailed risk governance structure of the bank, which is also applicable to Muzn is disclosed in the main Pillar III document of the bank. In addition, a dedicated Sharia Supervisory Board (SSB) has been established which reports to the Board of Directors of the bank and ensures Sharia compliance in the operations of Muzn.

Specifically, Muzn has exposure to the following risks.

- Credit risk
- Liquidity risk
- Market risk
- Operational risk
- Rate of return risk, and
- Displaced commercial risk

Credit Risk

Credit risk is the risk of financial loss to Muzn if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from Muzn's financings and advances to customers and other banks.

Corporate Credit:

Muzn manages and controls credit risk by setting internal limits on the amount of risk it is willing to accept for individual counterparties and groups (single obligors) and industry sectors in line with the guidelines of Central Bank of Oman.

Muzn has a conservative provisioning policy for its financings and provisions are made taking into account both the Central Bank's norms and international financial standards.

For risk management reporting purposes for the corporate portfolio, Muzn considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

Retail Credit:

Retail Credit Division manages the credit risk in the Muzn retail portfolio. The small retail credit portfolio is focused on Ijara, Murabaha and Diminishing Musharaka product programs approved by the Board Risk Committee. Both corporate and retail credit portfolios are monitored by the management through periodic performance reports which are presented to the Board Risk Committee.

Impairment Policy:

All financing contracts of Muzn are regularly monitored to ensure compliance with the stipulated repayment terms. These financings are classified into one of the 5 risk classification categories: Standard, Special Mention, Substandard, Doubtful, and Loss – as stipulated by Central Bank of Oman regulations and guidelines. Muzn creates provision for non-performing debts promptly, as and when required in line with the conservative provisioning norms it has set for itself and arrives at the provisioning requirement both under financial reporting framework and CBO guidelines and maintains whichever provision is higher. In addition to the above, Muzn also makes a general loan loss provision on the standard portfolio equivalent to 2% of retail lending portfolio and 1% of corporate portfolio.

(i) Total gross credit exposures over the period broken down by major types of credit exposure:

(RO'000)

Sl No	Type of Credit Exposure	Total Gross Exposure as at	
	Particulars (RO'000)	31-December-17	31-December-16
1	Deferred sale under Murabaha	**1,696**	1,773
2	Ijara Muntahia Bittamleek	**86,596**	85,155
3	Diminishing Musharaka	**11,119**	12,204
4	Forward Ijara	**4,703**	7,299
	Total	**104,114**	106,431

(ii) Geographic distribution of exposures by major types of credit exposure as at 31 December 2017:

As at 31 December 2017, all the credit exposures are within Oman only (2016: all exposures within Oman).

(iii) Industry or counter party type distribution of exposures, broken down by major types of credit exposure as at 31 December 2017:

(RO'000)

S. No	Economic Sector	Deferred sales under Murabaha	Ijara Muntahiah Bittamleek	Diminishing Musharaka	Forward Ijara	Total	Percentage composition	Off Balance sheet exposure**
1	Personal	1,334	60,944	546	3,271	66,096	64%	1,147
2	Construction	11	16,714	10,206	1,384	28,316	28%	871
3	Manufacturing	-	1,847	100	-	1,947	2%	-
4	Trade	232	-	-	-	232	0%	-
5	Services	88	5,947	156	-	6,191	6%	-
6	Others	-	-	-	-	-		699
	Total	**1,665**	**85,452**	**11,008**	**4,656**	**102,781**	**100%**	**2,717**

** Off balance sheet exposure relates to commitments under standard business norms, letter of credits & guarantees.

As at 31 December 2017, the assets were funded by IAH and shareholders in the following ratio:

IAH	85%
Shareholders	15%

(iv) Residual contractual maturity as at 31 December 2017 of the whole financing portfolio, broken down by major types of credit exposure:

(RO'000)

S. No	Time Band	Deferred sales under Murabaha	Ijara Muntahiah Bittamleek	Diminishing Musharaka	Forward Ijara	(RO'000) Total
1	Up to 1 month	52	1,142	82	231	1,507
2	1-6 months	292	4,361	1,063	246	5,962
3	6-12 months	230	4,464	870	572	6,136
4	5-1 years	1,034	34,055	7,152	3,607	45,848
5	Over 5 years	57	41,430	1,841		43,328
	Total	**1,665**	**85,452**	**11,008**	**4,656**	**102,781**

(v) Movement of gross finance

(RO'000)

Movement of Gross Finances during the year ended 31 December 2017							
S. No	Details	Performing Finances		Non-performing Finances			
		Standard	Special Mention	Sub-Standard	Doubtful	Loss	Total
1	Opening balance	103,916	1,736	-	780	-	106,432
2	Migration / changes (+/ -)	(14)	-	-	(780)	794	-
3	New Finances	15,569	-	-		-	15,569
4	Recovery of Financing	(17,887)	-	-	-	-	(17,887)
5	**Closing balance**	**101,584**	**1,736**	-	-	**794**	**104,114**
6	Provisions held	1,071	-	-	-	190	1,261
7	Reserve interest	-	-	-	-	72	72

(vi) Movement of Provisions and Reserve Profit

Particulars (RO'000)	2017	2016
Provision at beginning of the period	1,333	1,176
Charge / (Released) for the period	(33)	118
Reserve Profit for the period	33	39
Provision at end of the period	1,333	1,333

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Credit Risk –Disclosures for portfolios subject to the standardized approach.

Qualitative Disclosures:

- The bank is following Moody's rating for both sovereign and interbank exposures and the balance is treated as unrated at 100% risk.
- With the approval of the CBO, the bank uses the discretion to treat Finances as unrated at risk weight of 100%, except housing finances which are risk weighted at 35% based on the requirements as stipulated in the guidelines issued by CBO.
- Similarly, with the approval of CBO, the bank uses the discretion of the simple approach for recognising collaterals.

Quantitative Disclosures:

Gross exposure amount as at 31 December 2017, subject to the standardized approach is as below:

(RO'000)

Sr No	Product / Rating	Carrying 0%	Carrying 20%	Carrying 35%	Carrying 50%	Carrying 100%	Carrying 150%	Total
	Rated							
1	Sovereign	8,147	-	-	-	-	-	8,147
2	Banks	-	19,932	-	-	-	-	19,932
	Unrated							
1	Corporate	-	-	-	-	-	-	-
2	Retail	-	-	-	-	1,361	-	1,361
3	Claims secured by residential property	-	-	58,805	699	7,200	-	66,705
4	Claims secured by commercial property	-	-	-	-	36,701	-	36,701
5	Past due Financing	-	-	-	-	532	-	532
6	Other assets	1,085	-	-	-	2,359	-	3,444
7	Venture Capital & Private Equity Investments	-	-	-	-	-	-	-
8	Off-balance Sheet Items	-	-	-	-	-	-	-
	Total Banking Book	**9,232**	**19,932**	**58,805**	**699**	**48,153**	-	**136,822**

Credit Risk Mitigation

Credit risk mitigation refers to the use of a number of techniques, like collaterals and guarantees to mitigate credit risks that the Muzn is exposed to. Credit risk mitigates reduce the credit risk by allowing Muzn to protect against counterparty non-performance of credit contracts through collaterals, netting agreements and guarantees.

Qualitative Disclosure

The Bank only considers Sharia approved collaterals and guarantees to mitigate credit risk. Assets offered by the customer must meet the following criteria to be acceptable as collateral:

- Assets must be maintaining their value at the level prevalent at inception, until maturity of the facility approved;
- Such assets should be easily convertible into cash, if required;
- There should be a reasonable market for the assets; and
- Muzn should be able to enforce its right over the assets if necessary.

Currently Muzn undertakes ownership/joint ownership of assets provided by customers.

Collateral Management:

Muzn employs a range of policies and procedures to mitigate credit risk. The credit risk mitigates include collaterals like:

- Real estate
- Joint ownership

Collateral management is exercised for Muzn at the centralized level. A robust collateral management system is in place to mitigate any credit risk. The Bank has a strong credit administration process that ensures compliance with terms of approval, documentation and continuous review to ensure quality of credit and collaterals.

Securities obtained by way of legal mortgage over real estate to be valued at least once in 3 years or more frequently if situation warrants.

Liquidity Risk

Qualitative Disclosures:

Liquidity may be defined as a Muzn's ability to ensure the availability of funds to meet all on-balance sheet and off-balance sheet commitments at a reasonable price. Liquidity Risk can in turn be defined as the risk to earnings and capital arising from a Muzn's potential inability to meet its liabilities when they become due.

Besides its funding sources, Muzn enjoys the support of its Parent Bank in meeting some of its liquidity needs. The liquidity risk in Muzn is monitored through a regular reporting mechanism to the ALCO. In order to ensure that Muzn meets its financial obligations as and when they fall due, cash flow positions are closely monitored. Sufficient liquidity is required to be maintained by Banks not only for ensuring the continuation of operations, but also for the generation of earning assets and repayment of existing liabilities.

Liquidity ratios of Muzn (i.e. Liquid assets to total assets) are regularly monitored. The average ratio of liquid assets to total assets during the year for Muzn was 18.7% (as shown below). In addition, the cumulative gaps vis-à-vis cumulative liabilities prescribed by the Regulators/Internal Policies are monitored.

Muzn monitors its liquidity risk of funding related to current accounts and other equity with investment account holders on an individual basis as well as on an aggregate basis through cash flow and stock approach.

Treasury department of the Muzn window and the Asset Liability Committee (ALCO) controls and monitors the liquidity and ensures that the window is not exposed to undue liquidity risk and at the same time makes optimum use of its funds through Sharia compliant financing and investment activities.

Indicators of exposure to liquidity risk – short-term assets to short-term liabilities

Particular	RO
Short-term Assets	41,390
Short-term Liabilities	88,354
Short-term Assets to Liabilities	46.85%

Indicators of exposure to liquidity risk - liquid assets ratio

Particular	RO
Liquid Assets	25,201
Total Assets	134,304
Short-term Liabilities	88,354
Total Liabilities	123,213
Liquid Assets to Total Assets	18.76%
Liquid Assets to Short-term Liabilities	28.52%
Liquid Assets to Total Liabilities	20.45%

Quantitative Disclosures:

The maturity profile of the assets and liabilities in line with guidelines issued by Central bank of Oman, at 31 December 2017 was as follows:

	Due on demand and up to 30 days	More than 1 month to 6 months	More than 6 months to 12 months	More than 1 year to 5 years	Over 5 years	Total
31 December 2017	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Bank of Oman	2,207	1,395	454	547	666	5,269
financial institutions	19,932	-	-	-	-	19,932
Financial assets:						
- Held to Maturity	-	-	-	1,926	-	1,926
- Held for Trade	3,550	-	-	-	-	3,550
Deferred sales Murabaha	52	292	230	1,034	57	1,665
Ijarah Muntahiah Bittamleek – net	1,142	4,361	4,464	34,055	41,430	85,452
Diminishing Musharaka	82	1,063	870	7,152	1,841	11,008
Forward Ijarah	231	246	572	3,607	-	4,656
Property and equipment (net)	-	-	-	-	599	599
Other assets	247	-	-	-	-	247
Total assets	**27,856**	**7,357**	**6,590**	**47,908**	**44,593**	**134,304**
Current accounts	5,276	-	-	-	-	5,276
Other liabilities	3,481	-	-	-	-	3,481
Unrestricted investment account holders	18,625	46,233	14,739	13,872	20,987	114,456
Owner's equity	-	-	-	-	11,091	11,091
Total liabilities and Unrestricted investment accountholders and owners' equity	**27,382**	**46,233**	**14,739**	**13,872**	**32,078**	**134,304**

Market Risk

Qualitative Disclosures:

Market risk is the risk of a change in the actual or effective market value and earnings of a portfolio due to the adverse movements in market variables. The market variables inter-alia includes equity prices, bond price, commodity price and Foreign Exchange rates. The objective of Market Risk management is to facilitate business growth but operating at the optimal risk levels.

- As at 31 December 2017, Muzn has minimal exposure to market risk as:
- Muzn does not have material exposure in currencies other than Omani Riyal;
- Muzn does not hold trading positions in equity;
- Muzn has no position in commodities.

Market Risk arises from fluctuations in profit rates. There are no trading positions in equities or derivatives. The Muzn ALCO regularly monitors the portfolio of assets and liabilities in the banking book for any interest rate risks.

Operational Risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial losses. Muzn cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, Muzn is able to manage risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff training and assessment processes, including the use of internal audit.

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The bank follows basic indicator approach for determining operational risk.

The Capital charge for operational risk under Basic Indicator approach is calculated by taking the average of gross income multiplied by 15%, for each of the last three financial years, excluding years of negative or zero gross income. The gross income is Net profit income (+) other income (+) Provisions for unpaid profit (-) realized profit on sale of Available for Sale (AFS) investments (-) extraordinary / irregular items of income.

Capital Charge for Operational Risk under Basic Indicator Approach as per Basel II is RO (000s) 362.

The Risk weighted assets for operational risk as per Basel II is RO (000s) 4,572.

Insurance is another tool used by the bank as an operational risk mitigant. Insurance such as Bankers' Blanket Bond, Electronic and Computer Crimes, Professional Indemnity, incomplete transactions, etc as obtained by the bank aim at protecting the bank from high severity risks by reducing the financial impact of the same.

In addition to the above and in order to keep control of operational incidences / losses the bank has set in place a special operational risk framework against which incidents / losses are being monitored regularly for possible breaches and appropriate mitigates are put in place.

Rate of return risk

Qualitative Disclosures:

Rate of return risk refers to the possible impact on the net income of Muzn arising from the impact of changes in market rates and relevant benchmark rates on the return on assets and on the returns payable on funding. An increase in benchmark rates may result in IAH having expectation of a higher rate of return, while the returns on assets may be adjusting more slowly due to longer maturities, thereby affecting the net income of Muzn.

The profit distribution to Investment Accounts is based on profit sharing agreements. Therefore, Muzn is not subject to any significant profit rate risk. However, the profit sharing agreements will result in Displaced Commercial Risk (DCR) when Muzn' s results do not allow distribution of profits in line with market rates. To cater against DCR, Muzn creates a Profit Equalization Reserve.

Rate of return risk is managed by monitoring the sensitivity of the bank's financial assets and liabilities to various standardized profit rate shocks. Standardised shocks include a 100 basis point and 200 basis point parallel shifts in yield curves that are considered on a monthly basis. The impact of these shocks is analysed in the context of its impact on Earnings and Economic Value. The impact is compared against internal limits which have been formulated in line with the Central Bank of Oman and Basel Committee guidelines. The analysis is regularly reviewed by the Management and Board Risk Committee.

Quantitative Disclosures:

The assumptions used to measure the sensitivity is parallel shift in interest rate by 200 basis points (bps) to measure the profit sensitivity of earnings and profit rate sensitivity of capital.

As at December 2017	200 bps increase	200 bps decrease
Earnings impact - RO'000s	128	(128)

Muzn's profit sensitivity position, in line with guidelines issued by Central bank of Oman, based on contractual re-pricing arrangements at 31 December 2017 was as follows:

	Effective average profit rate	Due on demand and within 6 months	Due within 7 to 12 months	Due within 1 to 5 years	Due after 5 years	Non-profit bearing	Total
31 December 2017	%	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Bank of Oman ("CBO")	N/A	-	-	-	-	5,269	5,269
Due from banks and financial Institutions	1.3%	19,931	-	-	-	1	19,932
Financial assets:							
- Held to Maturity	6.5%	-	-	1,926	-	-	1,926
- Held for Trade	4.3%	3,550	-	-	-	-	3,550
Deferred sales under Murabah	4.7%	344	230	1,034	57	-	1,665
Ijarah Muntahia Bittamleek – net	5.3%	5,503	4,464	34,055	41,430	-	85,452
Diminishing Musharaka	5.3%	1,145	870	7,152	1,841	-	11,008
Forward Ijarah	N/A	-	-	-	-	4,656	4,656
Property and equipment – net	N/A	-	-	-	-	599	599
Other assets	N/A	-	-	-	-	247	247
Total assets		**30,473**	**5,564**	**44,167**	**43,328**	**10,772**	**134,304**
Current accounts	N/A	-	-	-	-	5,276	5,276
Other liabilities	N/A	-	-	-	-	3,481	3,481
Unrestricted investment accountholders	2.4%	64,858	14,739	13,872	20,640	347	114,456
Owners' equity	N/A	-	-	-	-	11,091	11,091
Total liabilities and owners' equity		64,858	14,739	13,872	20,640	20,195	134,304
On-balance sheet gap		(34,385)	(9,175)	30,295	22,688	(9,423)	-
Cumulative profit sensitivity gap		(34,385)	(43,560)	(13,265)	9,423	-	-

Displaced commercial risk

Displaced commercial risk refers to the magnitude of risks that are transferred to the shareholders of Muzn in order to cushion the Investment Account Holders (IAH) from bearing some or all of the risks to which they are contractually exposed to in Mudaraba funding contracts. Muzn creates and manages both PER and Investment risk reserve to smoothen IAH returns. Further, Muzn also adjusts its Mudarib share in order to smoothen returns of IAH.

Qualitative Disclosure:

The Bank has set up prudential reserve account to minimize the adverse impact of income smoothing for PSIA on its shareholders' returns and to meet potential but unexpected losses that would be borne by the IAH on investments financed by PSIA, namely:

Profit Equalization Reserve (PER)

PER comprises amounts appropriated out of the gross income from the Mudaraba to be available for smoothing returns paid to the IAH and the shareholders, and consists of a PSIA portion and a shareholders' portion;

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Investment Risk Reserve (IRR)

IRR comprises amounts appropriated out of the income of IAH after deduction of the Mudarib share of income, to meet any future losses on the investments financed by the PSIA.

An analysis of distribution during the year to IAH by Muzn is as follows:

Particular	Amount RO'000
Total profits available for distribution	4,512
Profit sharing	
- Muzn 's share as fund provider	1,371
- IAH	3,142
Profits for IAH before smoothening	3,142
Smoothening:	
- PER	(56)
- IRR	(25)
Profits paid out to IAH after smoothening	3,061

- During the period the Bank utilized OMR Nil (FY2016: Nil) from PER for the purpose of enhancing the returns to depositors
- The Bank is taking all the Risk Weighted Assets funded by IAH for the purpose of arriving at Total Risk Weighted Assets and capital requirement is calculated accordingly.

Quantitative Disclosures

Historical Rate of Return of IAH:

Historical Rate of Return of unrestricted Investment Accountholder:	2017	2016	2015	2014	2013
	RO'000	RO'000	RO'000	RO'000	RO'000
Profits available for distribution	4,512	3,674	1,349	405	184
Profit Distributed	3,061	1,536	591	269	122
Funds Invested	102,781	105,099	96,787	67,543	13,115
Rate as %age of fund invested	2.98%	1.46%	0.61%	0.40%	0.93%

Five years comparison of historical profit rates for unrestricted IAH.

	2017	2016	2015	2014	2013
Savings Account (Mudarabah)	0.70%	0.73%	0.79%	0.90%	0.50%
Flexi Wakala	0.10%	0.10%	0.10%	0.10%	0.10%
Flexi Wakala - Elite	2.25%	2.25%	2.25%	-	-
Flexi Wakala - Premium	1.75%	-	-	-	-
Wakala- Upto 6 months	0.10% - 0.25%	0.10% - 0.25%	0.10% - 0.25%	0.10% - 0.25%	0.10% - 0.35%
Wakala - > 6months to 1 Year	0.40% - 0.75%	0.40% - 0.75%	0.40% - 0.55%	0.35% - 0.50%	0.70% - 0.90%
Wakala - > 1 Year to 3 Years	1.75% - 2.50%	1.75% - 2.50%	0.75% - 1.75%	0.70% - 1.60%	1.20% - 2.20%
Wakala - > 3 Years	3.00% - 3.50%	3.00% - 3.50%	2.00% - 2.25%	1.80% - 2.00%	2.40% - 2.70%
Government Flexi Wakala	1.00%	0.50%	0.50%	0.50%	-

Contract Specific Risks

The Credit Risk Appetite document of Muzn has provided limits for the purpose of financing, it is defined within the purpose of financing are the various Shari'a compliant financing contracts that can be used. The risk weighting requirement for each of the Sharia compliant financing contracts, based on the risk profile of the customer as provided in the IBRF is taken into account for the purposes of computing the Capital Adequacy Ratio of Muzn.

Quantitative Disclosures:

Credit risk weighted assets by type of financing contracts is as follows:

Financing Contracts	Risk Weighted Assets Amount '000
Deferred sales Under Murabaha	1,696
Ijarah Muntahia Bittamleek	50,584
Diminishing Musharaka	10,761
Forward Ijarah	2,588
Letter of Guarantee	350
Letter of Credit	-
Total RWA of Financing Contracts	65,978

General Governance Disclosures

The CMA code of Corporate Governance for Public Listed Companies and the CBO guidelines as per IBRF Corporate Governance and Banking and Financial Institutions are the principal codes and drivers of Corporate Governance practices in the Sultanate of Oman. Muzn complies with all their provisions.

The following disclosure summarizes the disclosures of related party:

Deposits and other accounts	2017	2016
	RO'000	RO'000
Directors, Sharia Supervisors and shareholders holding less than 10% interest in Muzn	6940	7,574
Financings		
Directors, Sharia Supervisors and shareholders holding less than 10% interest in Muzn	120	6

Remuneration paid to Directors & Sharia Supervisors	2017 RO'000	2016 RO'000
Chairman		
– remuneration proposed	8	8
– sitting fees paid	3	3
– other expenses paid	3	3
Other Directors		
– remuneration proposed	19	16
– sitting fees paid	12	16
– other expenses paid	8	5
Management fee payable to conventional banking	60	53

Muzn maintains a formal procedure on handling of customer complaints. Complaints related to Muzn are dealt with by the conventional banking call center equipped with the required resources to respond to customer calls in a professional manner. The complaint management team of the Conventional Bank takes active part in resolution of customers' complaint and considers customers feedback on products and services. All complaints are logged and investigated by persons not directly related to the subject matter of the complaint.

Sharia Supervisory Board (SSB)

Muzn's independent Shari'a Supervisory Board is an external Shari'a Committee comprising of independent and well renowned Shari'a Scholars who guide and ensure that the operations, services and products offered by Muzn comply with the principles of Shari'a.

In case SSB rules any earnings Sharia non-compliant, such income is diverted to a charity account and disbursed to charitable organization. . Income generated from late payment charges (whereby client undertakes to donate to charity a certain amount in case of delay in installment payments) and whenever a transaction which is treated as Shari'a non-Compliant by Sharia Audit Unit and endorsed by SSB, the income from such shari'a non-compliant account becomes part of charity Account.

The Internal Sharia reviewer performs functions based on the shari'a guidelines provided by CBO in the IBRF, Sharia rulings and resolutions issued by SSB. Sharia audit includes continuous audit for transactions of all departments. Its observations and findings are reported in the Sharia audit report to SSB which is also conveyed and discussed with management, with documentation of management responses in addition to recommending action plan for each observation.

As per IBRF, Islamic banks are required to apply Accounting standards (Only and not the Shari'a Standards) issued by AAOIFI and abide by the comprehensive IBRF regulatory framework and guidelines.

Muzn's Sharia Supervisory Board consists of following members namely:

Sheikh Dr. Mohamed Bin Ali Elgari is a Professor of Islamic Economics at King Abdulaziz University, Saudi Arabia. He is an Expert at the Islamic Jurisprudence Academy of the Organization of Islamic Cooperation (OIC) and the Islamic Jurisprudence Academy of the Islamic World League. Sheikh Elgari is also a member of the Sharia Council of Accounting and Auditing Organization for Islamic Financial Institutions (AAOFI), Chairman Sharia Supervisory Board of Muzn Islamic Banking Services and Sharia Board Member of several reputable Islamic Banks and Takaful Companies across the globe.

Sheikh Datuk Dr. Mohamed Daud Bakar is a Malaysian Sharia Scholar and Chairman of the Central Sharia Advisory Council of the Central Bank of Malaysia and Securities Commission of Malaysia. Sheikh Bakar's area of specialization includes Islamic Legal Theory, Islamic Banking and Finance and Islamic Law of Zakah. Datuk Dr. Bakar has published more than 30 articles in academic journals while also being a member of several Sharia Boards for Banks and Islamic financial institutions worldwide.

Sheikh Saleh Al Kharusi is a Director of the Notary Public Office Ministry of Justice and a part-time lecturer of Sharia sciences. Sheikh Saleh has bachelor's degree in Shari'a from the Institute of Shari'a Sciences in the Sultanate of Oman and a Master's Degree in Financial Transaction from Sultan Qaboos University

Dr. Khalid Said Al Aamri, an Assistant professor at Sultan Qaboos University. Dr. Al-Amri serves as an advisor to the board of director at Al Madina Takaful and a member in the Audit Committee. He has done extensive research in the area of finance, Takaful insurance, and financial risk management. His research interests focus on finance, corporate governance, Takaful insurance, and, Risk Management. He also serves as an ad hoc referee for international academic journals. He has published in a number of internationally refereed journals and delivered presentations at international renowned conferences. He has been awarded a best paper award in Western Risk and Insurance in USA. Dr. Al-Amri is a member of American Risk and Insurance Association (ARIA). He is also a Certified Sharia Advisor and Auditor from AAOIFI - Accounting and Auditing Organization for Islamic Financial Institutions.

H.H Sayyid Dr. Adham Turki Al Said, is an Assistant Professor of Economics at Sultan Qaboos University in Oman. Dr. Adham is a Chairman of Board of Trustees, Scientific College of Design. He is also a member in several government and private organizations such as Partner, The Firm for Business and Economic Consulting and he provided a proposal on SME to Shura Council in 2014. Dr. Adham has a Ph.D. in Economics from University of Western Australia, Australia — 2011.

There were a total of four SSB meetings held in 2017. Date of the meetings and attendance of each SSB Member is follows:

Name of the Board Member	Date of Meeting and attendance			
	28/03/2017	23/05/2017	12/09/2017	13/12/2017
Sheikh Dr. Mohamed Bin Ali Elgari- Chairman	√	√	√	√
Sheikh Datuk Dr. Mohammed Daud Bakar	√	√	√	√
Sheikh Saleh Al Kharusi	√	√	√	√
H.H Sayyid Dr. Adham Al Said Non-Voting Member	√	√	√	√
Dr. Khalid Said Al Amri Non-Voting Member	√	√	√	√

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Remuneration for Sharia Supervisory Board Members in 2017:

Total Remuneration paid to the five Scholars for the year 2017 was OMR 42,350.000. The breakup is as follows:-

Name of the Board Member	Total Fees(RO)
Sheikh Dr. Mohamed Bin Ali Elgari	10,780.000
Sheikh Datuk Dr. Mohammed Daud Bakar	8,855.000
Sheikh Saleh Al Kharusi	8,855.000
Dr. Khalid Said Al Amri Non-Voting Member	6,930.000
H.H Sayyid Dr. Adham Al Said Non-Voting Member	6,930.000

Sharia compliance key controls

Sharia compliance is ensured in day to day business of Muzn through the following key controls:

- All the products being offered by Muzn are approved by the SSB;
- All investments made by Muzn are approved by SSB;
- The Fatawa approving such products are available on the website of Muzn;
- The responsibility of payment of zakat is on individual shareholders and investment account holders;
- There has been no non-compliance with Sharia rules and regulations during the year;
- Muzn has in place a Sharia Compliance Unit (SCU) which facilitates the management in ensuring compliance with Sharia (as manifested by the guidelines and Fatawa issued by the SSB) and Islamic banking stipulations of the Central Bank on a day to day basis in all its business activities, operations and transactions. This is achieved through review and approval of the contracts, agreements, policies, procedures, products, process flows, transactions, reports (profit distribution calculations), etc;
- Templates of agreements used by Muzn are approved by SSB;
- Islamic banking knowledge and experience is considered to be a compulsory requirement for hiring of staff handling core Muzn functions; staff has been provided training throughout the year on Sharia matters;

Disclosure of the nature, size and number of violations of Sharia compliance during the year:

There is no violation to SSB's Sharia ruling and AAOIFI Sharia standard have been found during the year.

Disclosure of annual Zakah contributions of the Licensee, where relevant, according to constitution, general assembly or national requirements or as required by the respective SSB

SSB issues its Sharia compliance certificate where it identifies that Sharia compliance has been observed in the bank's transactions and contracts, and in case of any violation, the observation is listed in the report. In addition, and as per Management decision, SSB certificate also stipulates that Zakat calculation and payment is the responsibility of the shareholders.

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Social service and customer education

Muzn Islamic Banking is continuously providing education to customers and engaged in social service activities. In past couple of years, Muzn held Shari'a forums in Salalah, Sur and Muscat regions under its SSB to create awareness about local community. The website of Muzn has sections for brief detail of products and FAQs on Islamic Banking for imparting knowledge regarding Islamic Banking. Muzn's staffs are well trained in Islamic banking and they educate customers about Islamic banking and about Shari'a Compliant products in detail.

Muzn Islamic Banking as part of National Bank of Oman distributes food hampers to the poor and needy people in the holy month of Ramadan. A team of volunteers including the senior management team delivered several food hampers to low income families across the Muscat Governorate to inaugurate this initiative.

BASEL III – Transition Disclosure:

Further to the Guidelines on composition of capital disclosure requirements (CP1 & CP2) issued by Central Bank of Oman, the following are the mandatory disclosures for the year ended 31 December 2017.

Basel III common disclosure template to be used during the transition of regulatory adjustments (i.e. from 1 January 2013 to 1 January 2018) (RO '000)

	AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT
Common Equity Tier 1 capital: instruments and reserves	
Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	13,500
Retained earnings	(2,409)
Accumulated other comprehensive income (and other reserves)	
Public sector capital injections grandfathered until 1 January 2018	-
Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-
Common Equity Tier 1 capital before regulatory adjustments	**11,091**
Common Equity Tier 1 capital: regulatory adjustments	
Deferred tax assets arising from temporary differences (net of related tax liability)	-
National specific regulatory adjustments of which: Shortfall in MCR of Islamic Banking window and foreign branches of the bank	-
Total regulatory adjustments to Common equity Tier 1	
Common Equity Tier 1 capital (CET1)	**11,091**
Additional Tier 1 capital: instruments - NIL	
Additional Tier 1 capital: regulatory adjustments	
Total regulatory adjustments to Additional Tier 1 capital	-
Additional Tier 1 capital (AT1)	
Tier 1 capital (T1 = CET1 + AT1)	**11,091**
Tier 2 capital: instruments and provisions	
Directly issued qualifying Tier 2 instruments plus related stock surplus	-
Directly issued capital instruments subject to phase out from Tier 2	-
Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	-
of which: instruments issued by subsidiaries subject to phase out	-
General Provisions	913
Tier 2 capital before regulatory adjustments	**913**
Tier 2 capital: regulatory adjustments	
National specific regulatory adjustments	-
REGULATORY ADJUSTMENTS APPLIED TO TIER 2 IN RESPECT OF AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT.	-
OF WHICH: Cumulative fair value gains or losses on available for sale instruments	-
Total regulatory adjustments to Tier 2 capital	-
Tier 2 capital (T2)	**913**
Total capital (TC = T1 + T2)	**12,004**
Total risk weighted assets	**77,646**
Of which: Credit risk weighted assets	73,071
Of which: Market risk weighted assets	3
Of which: Operational risk weighted assets	4,572
Capital Ratios	
Common Equity Tier 1 (as a percentage of risk weighted assets)	**14.28**
Tier 1 (as a percentage of risk weighted assets)	**14.28**
Total capital (as a percentage of risk weighted assets)	**15.46**
Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus G-SIB/D-SIB buffer requirement expressed as a percentage of risk weighted assets)	
of which: capital conservation buffer requirement	
of which: bank specific countercyclical buffer requirement	
of which: D-SIB/G-SIB buffer requirement	
Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets)	
National minima (if different from Basel III)	
National Common Equity Tier 1 minimum ratio (if different from Basel 3 minimum)	8.250
National Tier 1 minimum ratio (if different from Basel 3 minimum)	10.250
National total capital minimum ratio (if different from Basel 3 minimum)	**13.250**
Total Investment account holders	
Amount of investment account holders funds	**114,108**
Profit equalization reserve	**254**
Investment risk reserve	**93**
Total Investment account holders	**114,456**

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Balance sheet as in published financial statements RO'000s

	Balance sheet as in published financial statements 31-Dec-17
Assets	
Cash and balances with Central Bank of Oman	5,269
Certificates of deposit	-
Due from banks	19,932
Financing to banks	-
Financing to Customers	102,781
Investments	5,476
Property and equipment	599
Deferred tax assets	-
Other assets	247
Total assets	**134,304**
Liabilities	
Due to banks	-
Customer deposits	119,732
Euro medium term notes	-
Other liabilities	3,482
Subordinated bonds	-
Total liabilities	**123,213**
Shareholders' Equity	
Paid-upshare capital	13,500
Share premium	-
Legal reserve	-
General reserve	-
Retained earnings	(2,409)
Other reserves	-
Cumulative changes in fair value of investments	-
Subordinated debt reserve	-
Tier 1 perpetual bond	-
Total shareholders' equity	**11,091**
Total liability and shareholders' funds	**134,304**

Balance sheet as in published financial statements expanded RO'000s

	Balance sheet as in published financial statements 31-Dec-17	Reference
Assets		
Cash and balances with Central Bank of Oman	5,269	
Certificates of deposit	-	
Balance with banks and money at call and short notice	19,932	
Investments	5,476	
Financing Of which :		
Financing to Banks - Gross	-	
General Provisions considered for Tier 2	-	
Net Financing to banks	-	
Financing to Customers - Gross	104,114	
Specific Provisions & Reserved Profits	(262)	
General Provisions considered for Tier 2	(913)	A1
General Provisions not considered for Tier 2	(157)	
Net Financing to customers	102,781	
Fixed assets	599	
Other assets of which:	247	
Deferred tax assets	-	
Amount considered for CET1		
Current year allocation - not eligible	-	
Total Assets	**134,304**	
Capital & Liabilities		
Paid-up Capital	-	
Of which:		
Amount eligible for CET1	13,500	C1
Amount eligible for AT1	-	
Reverses and Surplus	(2,409)	
Of which: Amount eligible for CET1		
Retained earnings carried forward	(2,352)	C2
Profit for current year not eligible	(57)	
Legal reserve	-	
General reserve	-	
Subordinated debt reserve	-	
Proposed Stock Dividend	-	
Total Amount eligible for CET1	-	
Tier 1 perpetual bond	-	

Balance sheet as in published financial statements expanded RO'000s

	Balance sheet as in published financial statements 31-Dec-17	Reference
Proposed Cash Dividend	-	
Cumulative changes in fair value of investments	-	
Amount eligible for Tier 2	-	
Revaluation reserve	-	
Total Capital	**11,091**	
Deposits Of which:		
Deposits from banks	-	
Customer deposits	119,732	
	-	
Euro medium term notes	-	
Other deposits (Sub-debt)	-	
Other liabilities & provisions Of which:	3,482	
TOTAL	**134,304**	

Basel III common disclosure template to be used during the transition of regulatory adjustments (RO '000)

	Component of regulatory capital reported by bank	Source based on reference numbers/letters of the balance sheet under the regulatory scope of consolidation from step 2
Common Equity Tier 1 capital: instruments and reserves		
Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	13,500	C1
Retained earnings	(2,409)	C2
Accumulated other comprehensive income (and other reserves)	-	
Public sector capital injections grandfathered until 1 January 2018	-	
Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-	
Common Equity Tier 1 capital before regulatory adjustments	**11,091**	
Common Equity Tier 1 capital: regulatory adjustments		
Deferred tax assets arising from temporary differences (net of related tax liability)	-	
Total regulatory adjustments to Common equity Tier 1	-	
Common Equity Tier 1 capital (CET1)	**11,091**	
Additional Tier 1 capital: instruments (TIER1 PERPETUAL BOND)	-	

Basel II and III - Pillar III Report 2017

Basel III common disclosure template to be used during the transition of regulatory adjustments (RO '000)

	Component of regulatory capital reported by bank	Source based on reference numbers/letters of the balance sheet under the regulatory scope of consolidation from step 2
Additional Tier 1 capital: regulatory adjustments - Nil		
Tier 1 capital (T1 = CET1 + AT1)	11,091	
Tier 2 capital: instruments and provisions		
Directly issued qualifying Tier 2 instruments plus related stock surplus	-	
Directly issued capital instruments subject to phase out from Tier 2	-	
Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	-	
of which: instruments issued by subsidiaries subject to phase out	-	
General provisions	913	A1
Cumulative fair value gains or losses on available for sale instruments	-	
Tier 2 capital before regulatory adjustments	913	
Tier 2 capital: regulatory adjustments		
National specific regulatory adjustments	-	
REGULATORY ADJUSTMENTS APPLIED TO TIER 2 IN RESPECT OF AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT.	-	
OF WHICH: Cumulative fair value gains or losses on available for sale instruments	-	
Total regulatory adjustments to Tier 2 capital	-	
Tier 2 capital (T2)	**913**	
Total capital (TC = T1 + T2)	**12,004**	

Disclosure template for main features of all regulatory capital instruments

1. Common Equity.
Common equity comprises of assigned capital amounting to RO 13,500,000 transferred from National Bank of Oman SAOG.

2. All other regulatory capital instruments - Nil
This report on Basel II & III disclosures set out from pages no 1 to 24 was authorized for issue on 28th January 2018.

RAWAN BINT AHMED AL SAID
Chairperson

EY
Building a better working world

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PR No. HMH/15/2015; HMA/9/2015

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF OMAN SAOG (the "Bank")

Report on the financial statements

We have audited the accompanying statement of financial position of Muzn Islamic banking - Window of National Bank of Oman (the "Islamic Window) as of 31 December 2017, and the related statements of income, changes in owners' equity, cash flows and sources and uses of charity fund for the year then ended, and a summary of significant accounting policies and other explanatory information. These financial statements and the Bank's undertaking to operate its Islamic Window in accordance with Islamic Shari'a Rules and Principles as determined by the Shari'a Supervisory Board are the responsibility of the Bank's Board of Directors. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Islamic Window as of 31 December 2017, the results of its operations, changes in owners' equity, cash flows and sources and uses of charity fund for the year then ended in accordance with the Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Islamic Window of the Bank and the Financial Accounting Standards issued by AAOIFI.

Ernst & Young LLC

Muscat
10 March 2018

ERNST & YOUNG LLC
C.R. No. 1224013
P.O. Box 1750 - P.C. 112, Sultanate of Oman

STATEMENTS OF FINANCIAL POSITION

As at 31 December 2017

2016 USD'000	2017 USD'000		Note	2017 RO'000	2016 RO'000
		ASSETS			
39,125	**13,686**	Cash and balances with Central Bank of Oman ("CBO")	5	**5,269**	15,063
30,660	**51,771**	Due from banks and financial institutions	6	**19,932**	11,804
		Financial assets:			
2,501	**5,003**	- Held to Maturity	7	**1,926**	963
7,793	**9,221**	- Held for Trade	7	**3,550**	3,000
4,494	**4,325**	Deferred sales under Murabaha	8	**1,665**	1,730
218,340	**221,953**	Ijarah Muntahia Bittamleek - net	9	**85,452**	84,061
31,382	**28,592**	Diminishing Musharaka	10	**11,008**	12,082
18,769	**12,094**	Forward Ijarah	11	**4,656**	7,226
1,008	**1,556**	Property and equipment - net	12	**599**	388
678	**641**	Other assets	13	**247**	261
354,750	**348,842**	**TOTAL ASSETS**		**134,304**	136,578
		LIABILITIES, UNRESTRICTED INVESTMENT ACCOUNT HOLDERS AND OWNERS' EQUITY			
		LIABILITIES			
12,649	**13,704**	Current accounts		**5,276**	4,870
5,657	**9,042**	Other liabilities	14	**3,481**	2,177
18,306	**22,746**	**TOTAL LIABILITIES**		**8,757**	7,047
307,488	**297,288**	Unrestricted Investment Accountholders	16	**114,456**	118,383
		OWNERS' EQUITY			
35,065	**35,065**	Assigned capital	17	**13,500**	13,500
(6,109)	**(6,257)**	Accumulated losses		**(2,409)**	(2,352)
28,956	**28,808**	**TOTAL OWNERS' EQUITY**		**11,091**	11,148
354,750	**348,842**	TOTAL LIABILITIES, UNRESTRICTED INVESTMENT ACCOUNT HOLDERS AND OWNERS' EQUITY		**134,304**	136,578

The financial statements were approved by the Board of Directors on 28th January 2018

Chairperson

Chief Executive Officer

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2017

2016 USD'000	2017 USD'000		Note	2017 RO'000	2016 RO'000
		INCOME			
252	**223**	Deferred sales under Murabaha	18	**86**	97
8,851	**10,714**	Ijarah Muntahia Bittamleek	19	**4,125**	3,408
1,431	**1,717**	Diminishing Musharaka	20	**661**	551
36	**366**	Inter-Bank Wakala		**141**	14
10,570	**13,020**	**INCOME FROM JOINTLY FINANCED ASSETS**		**5,013**	4,070
		Less:			
(3,990)	**(7,951)**	Return on unrestricted investment accountholders	21	**(3,061)**	(1,536)
(66)	**(145)**	Profit equalization reserve		**(56)**	(25)
(28)	**(65)**	Investment risk reserve		**(25)**	(11)
(4,084)	**(8,161)**			**(3,142)**	(1,572)
6,486	**4,859**	**MUZN'S SHARE IN INCOME FROM INVESTMENT AS MUDARIB AND RABUL MAAL**		**1,871**	2,498
382	**590**	Investment income		**227**	147
314	**478**	Revenue from banking services		**184**	121
42	**99**	Foreign exchange gains–Net		**38**	15
7,224	**6,026**	**TOTAL OPERATING REVENUE**		**2,320**	2,781
(5,610)	**(5,545)**	**General and administrative expenses**	22	**(2,135)**	(2,160)
(306)	**(25)**	**Provisions for credit loss finances**		**(9)**	(118)
-	**110**	**Recoveries and release from provions of credit loss finances**	15	**42**	-
(644)	**(714)**	**Depreciation**	12	**(275)**	(248)
(6,560)	**(6,174)**	**TOTAL OPERATING EXPENSES**		**(2,377)**	(2,526)
664	**(148)**	**NET PROFIT (LOSS) FOR THE YEAR**		**(57)**	255

The notes 1 to 28 form part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

	Share capital RO'000	Accumulated losses RO'000	Total RO'000
Balance at 1 January 2017	**13,500**	**(2,352)**	**11,148**
Net loss for the year	**-**	**(57)**	**(57)**
Balance at 31 December 2017	**13,500**	**(2,409)**	**11,091**
Balance at 31 December 2017 (USD'000)	**35,065**	**(6,257)**	**28,808**
Balance at 1 January 2016	13,500	(2,607)	10,893
Net profit for the year	-	255	255
Balance at 31 December 2016	13,500	(2,352)	11,148
Balance at 31 December 2016 (USD'000)	35,065	(6,109)	28,956

The notes 1 to 28 form part of these financial statements.

STATEMENT OF CASH FLOWS

For the year ended 31 December 2017

2016 USD'000	2017 USD'000		2017 RO'000	2016 RO'000
		OPERATING ACTIVITIES		
664	(148)	Net profit (loss) for the year	(57)	255
		Adjustments for:		
644	714	Depreciation	275	248
306	25	Provisions for credit loss finances	9	118
-	(110)	Recoveries and release from provisions of credit loss finances	(42)	-
66	145	Profit equalization reserve	56	25
28	64	Investment risk reserve	25	11
1,708	690	Operating cash flow before changes in operating assets & liabilities	266	657
1,055	171	Changes in deferred sales under Murabaha assets and liabilities	66	406
(22,868)	(3,743)	Ijarah Muntahia Bittamleek assets	(1,441)	(8,804)
(782)	2,792	Diminishing Musharaka assets	1,075	(301)
600	6,678	Forward Ijarah assets	2,571	231
(70)	36	Other assets	13	(27)
(20,694)	1,055	Customer 's current accounts	406	(7,967)
1,322	3,387	Other liabilities	1,304	509
(39,729)	11,066	Net cash from/(used in) operating activities	4,260	(15,296)
		INVESTING ACTIVITIES		
-	(2,501)	Investment in financial asset held for maturity	(963)	-
(2,501)	(1,429)	Investment in financial asset held for trading	(550)	(963)
(481)	(1,262)	Purchase of property and equipment	(486)	(185)
(2,982)	(5,192)	Net cash (used in) investing activities	(1,999)	(1,148)
		FINANCING ACTIVITIES		
73,797	(10,200)	Movement in unrestricted investment account holders	(3,927)	28,412
73,797	(10,200)	Net cash (used in) from financing activities	(3,927)	28,412
31,086	(4,326)	(Decrease) in cash and cash equivalents	(1,666)	11,968
38,699	69,784	Cash and cash equivalents at the beginning of the year	26,867	14,899
69,785	65,457	CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	25,201	26,867
		REPRESENTING:		
39,125	13,686	Cash and balances with Central Banks	5,269	15,063
30,660	51,771	Due from banks and financial institutions	19,932	11,804
69,785	65,457		25,201	26,867

The notes 1 to 28 form part of these financial statements.

STATEMENT OF SOURCES AND USES OF CHARITY FUND

For the year ended 31 December 2017

2016 USD	2017 USD		2017 RO	2016 RO
-	-	Balance as at 1 January	-	-
		Non-Islamic income for the year		
4,199	4,995	Late payment penalties	1,923	1,617
4,199	4,995	Total source	1,923	1,617
		Use of charity fund:		
(2,099)	(1,665)	Oman Association for Disabled	(641)	(808)
(2,099)	(1,665)	Oman Society for the hearing impaired	(641)	(808)
-	(1,665)	Omani Association for Elderly Friends	(641)	-
-	-	Undistributed charity fund	-	-

1. LEGAL STATUS AND PRINCIPAL ACTIVITIES

Muzn Islamic Banking – Window of National Bank of Oman SAOG ('Muzn') was registered in the Sultanate of Oman as a window of National Bank of Oman SAOG. Muzn's principle place of business is in Muscat, Sultanate of Oman.

Muzn's operations commenced on 17 January 2013 and it currently operates through six branches in the Sultanate under the license issued by the Central Bank of Oman on 15 January 2013.

The principle activities of Muzn are taking demand, saving and deposit accounts, providing Murabaha finance, Ijarah financing, Musharaka financing and other Sharia compliant forms of financing as well as managing investor's money on the basis of Mudaraba or agency for a fee, providing commercial banking services and other investment activities.

Muzn's activities are regulated by the Central Bank of Oman ('CBO') and supervised by Sharia Supervisory Board ('SSB') comprising of five members.

Muzn's address is PO Box 751 and PC 112, Muscat, Sultanate of Oman.

Muzn employed 66 employees as at 31 December 2017 (2016: 70).

2. BASIS OF PREPARATION

2.1 Statement of compliance

The financial statements of Muzn Islamic Banking have been prepared in accordance with Financial Accounting Standards ('FAS') issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), the Sharia rules and principles as determined by the Sharia Supervisory Board of Muzn and the applicable laws and regulations issued by the CBO. In accordance with the requirements of IBRF, for accounting matters which are not covered by the AAOIFI standards, Muzn uses the relevant International Financial Reporting Standards ('IFRS') issued by the International Accounting Standards Board (IASB).

These financial statements relate to the Islamic Window operation only and do not include the financial results of the Bank. The complete set of Bank's financial statements are presented separately.

Statement of restricted investment accountholders and statement of Qard fund and Zakat are not presented as these are not applicable/relevant to Muzn's operations.

2.2 Basis of measurement

The financial statements are prepared on historical cost basis.

2.3 Functional and presentation currency

The financial statements have been presented in Rial Omani (RO) which is the functional currency of Muzn. Except as otherwise indicated, financial information presented has been rounded off to the nearest thousand Rial Omani (RO).

2.4 Use of estimates and judgements

The preparation of financial statements in conformity with AAOIFI requires management to make judgments estimates and assumptions that effect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements are described in note 4.

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set below have been consistently applied in dealing with items that are considered material in relation to Muzn's financial statements to the period presented.

Muzn Islamic Banking
Notes to Financial Statement 2017

3.1 Foreign currency translations

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in income statement.

Figures are also presented in United States Dollar (USD) for statement of financial position, income statement, statement of changes in equity, statement of cash flows and statement of sources and uses of charity fund, which have been translated from Rial Omani at an exchange rate of RO 0.385 to each US Dollar.

3.2 Financial instruments

3.2.1 Recognition

Muzn recognises Islamic financial assets and liabilities on the date at which they originated. Regular way purchases and sales of financial assets are recognised on the trade date at which Muzn commits to purchase and sell the asset. All other financial assets and liabilities (including assets and liabilities at fair value through profit or loss) are initially recognised on the trade date at which Muzn becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value, plus for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

3.2.2 Derecognition

A financial asset (or, where applicable a part of a financial asset or part of a group of similar assets) is derecognized when:

(i) the right to receive cash flows from the asset has expired;

(ii) Muzn has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A financial liability is derecognized when the obligation specified in the contract is discharged, cancelled or expires.

3.2.3 Measurement

Financial assets are measured initially at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss.

Subsequent to initial recognition all financial assets are measured at fair value, except equity instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably measured is stated at cost, including transaction costs, less impairment losses.

All non-trading financial liabilities are measured at amortised cost less impairment losses. Amortised cost is calculated on the effective profit rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective profit rate of the instrument.

3.3 Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash on hand, non-restricted cash deposited with the Central Bank of Oman and, amounts due from other Banks.

3.4 Offsetting

Financial assets and liabilities are offset and the net amount is reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously. Further, this should also be as per the Sharia principles and guidelines.

Income and expenses are presented on a net basis only for permitted transaction.

3.5 Deferred sales under Murabaha

Deferred sales under Murabaha are stated net of deferred profits and provisions for impairment. Muzn considers the promise made in the deferred sales to the purchase orderer as obligatory.

3.6 Ijarah Muntahia Bittamleek assets and Forward Ijarah

Ijarah Muntahia Bittamleek assets are initially recorded at cost. Ijarah Muntahia Bittamleek is a lease whereby the legal title of the leased asset passes to the lessee at the end of the Ijarah (lease term), provided that all Ijarah instalments are settled.

Depreciation is calculated using the straight-line method on all Ijarah Muntahia Bittamleek assets, at rates calculated to write off the cost of each asset over its useful life.

Forward Ijarah assets are recognised as assets at cost during the period of construction.

3.7 Diminishing Musharaka

Musharaka contract represents a partnership between Muzn and a customer whereby each party contributes to the capital in equal or varying proportions to develop a new asset or share an existing one, and whereby each of the party becomes an owner of the capital on a permanent or declining basis and shall have a share of profits or losses.

These are stated at the fair value of consideration given less any amounts written off and provision for impairment, if any. In Diminishing Musharaka based transactions, Muzn enters into a Musharaka based on Shirkat-ul-milk for financing an agreed share of fixed asset (e.g. house or land) with its customers and enters into periodic profit payment agreement on Ijara basis for the utilisation of Muzn's Musharaka share by the customer.

Over the tenor, one partner's investment in the partnership declines on account of the other partner's increase in the partnership investment through repayment of the former partner's share.

3.8 Property and equipment

Items of property and equipment are stated at cost less accumulated depreciation and impairment loss. Depreciation is calculated so as to write off the cost of property and equipment, by equal instalments over their estimated economic useful lives from the date the asset is brought into use, as follows:

Nature of Assets	Useful Life in Years
Furniture and fixtures	10
Equipment	5
Motor vehicles	4
Leasehold improvements	3

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each statement of financial position date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit. Repairs and renewals are charged to income statement when the expense is incurred. Subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the item of property and equipment. All other expenditure is recognized in income statement as an expense when incurred.

3.9 Unrestricted investment accountholders

All unrestricted investment accounts will be carried at cost plus profit attributable to unrestricted investment account holders and related reserves, less amounts settled.

Unrestricted investment account holders' share of income will be calculated based on the income generated from investment accounts after deducting Mudarib share. Operating expenses will be charged to shareholders' funds and not included in the calculation.

The basis applied by Muzn in arriving at the unrestricted investment account holders' share of income will be (total income from jointly financed Islamic finances less shareholders' income). Pre agreed profit share generated from unrestricted investment account holders will be deducted as Mudarib share and the remaining will be distributed to the unrestricted investment account holders.

3.10 Investment risk reserve

Investment risk reserves are amounts appropriated out of the income of unrestricted investment account holders, after allocating the Mudarib share, in order to cater against future losses for unrestricted investment account holders.

3.11 Profit equalization reserve

Muzn appropriates a certain amount in excess of the profit to be distributed to unrestricted investment accounts before taking into consideration the Mudarib share of income. This will be used to maintain a certain level of return on investment for unrestricted investment account holders.

3.12 Provisions

Provisions are recognized when Muzn has a present obligation (legal or constructive) arising from a past event and the costs to settle the obligation are both probable and able to be measured reliably.

According to the regulations of the Central Bank of Oman; Banks are required to have general credit loss provisions, at least equivalent to 1% of the total financing and interbank 0.5% categorized as Standard and Special Mention. However, for personal finance a minimum general loss provision of 2% of the Standard and Special Mention is required to address the heightened inherent risk.

3.13 Dividends

Dividends are recognized as a liability in the year in which they are declared.

3.14 Earnings prohibited by shari'a

Muzn is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a charity fund where Muzn disburses these funds according to the Sharia Supervisory Board's supervision and instructions.

3.15 Zakah

The responsibility of payment of zakah is on individual shareholders and investment account holders.

3.16 Joint and self-financed

Financing and receivables that are jointly owned by Muzn and the unrestricted investment accounts holders will be classified under the caption "jointly-financed" in the financial statements. Financing and receivables that are financed solely by Muzn will be classified under "self-financed".

3.17 Funds for Muzn

Muzn functions with funds specifically available for its Islamic banking activities and there is no commingling of funds with conventional banking business.

3.18 Revenue recognition

3.18.1 Deferred sales under Murabaha

Where the income is quantifiable and contractually determined at the commencement of the contract, income will be recognized on a time-apportioned basis over the period of the contract based on the principal amounts outstanding. Where the income from a contract is not quantifiable or contractually determinable, it will be recognized when realized. Income related to non performing accounts will be excluded from the income statement.

3.18.2 Diminishing Musharaka

Income from Musharaka is recognized when the right to receive payment is established or when distribution is made.

3.18.3 Ijarah Muntahia Bittamleek

Income from Ijarah Muntahia Bittamleek will be recognised on a time-apportioned basis over the lease term, net of depreciation. Income related to non performing Ijarah Muntahia Bittamleek assets will be excluded from the income statement.

3.18.4 Dividends

Dividends will be recognised when the right to receive payment is established.

3.18.5 Fee and Commission Income

Fee and commission income will be recognised when earned.

3.18.6 Muzn's Share as a Mudarib

Muzn's share as a Mudarib for managing unrestricted investment accounts will be accrued based on the terms and conditions of the related Mudaraba agreements.

3.18.7 Income allocation

Income from jointly financed activities will be allocated proportionately between unrestricted investment accounts and shareholders on the basis of the average balances outstanding during the year.

3.19 Taxation

Muzn is not taxable on a stand-alone basis as per the prevailing tax laws.

National Bank of Oman SAOG is taxable on a consolidated basis i.e including Muzn's financial results, accounted for as per the International Financial Reporting Standards. Accordingly, no current tax and deferred tax has been accounted for in these financial statements.

3.20 Employee benefits

End of service benefits are accrued in accordance with the terms of employment of the Muzn's employees at the statement of financial position date, having regard to the requirements of the Oman Labour Law. Employee entitlements to annual leave and leave passage are recognized when they accrue to employees and an accrual is made for the estimated liability arising as a result of services rendered by employees up to the statement of financial position date.

Contributions to a defined contribution retirement plan and occupational hazard insurance for Omani employees in accordance with the Omani Social Insurances Law of 1991 and its subsequent amendments are recognized as an expense in income statement as incurred.

3.21 Segment reporting

An operating segment is a component of Muzn that engages in business activities from which it may earn revenues and incur expenses including revenue and expenses that relate to transactions with any of the Muzn's other components whose operating results are reviewed regularly by the management to make decisions about the resources allocated to each segment and asses its performance and for which discrete financial information is available. Muzn's primary format for reporting segmental information is business segment, based upon management internal reporting structure. Muzn's main business segments comprise of retail, corporate and treasury operations.

3.22 Sharia supervisory board

All business activities, products, transactions, agreements, contracts and other relevant documents are subject to the supervision of the Sharia Supervisory Board of Muzn, which meets four times a year and consists of two prominent Sharia scholars as voting members and three non-voting members who are expert in the field. The SSB members appointed for a period of three years are:

- Sh. Dr. Mohamed Bin Ali Elgari – Chairman
- Dr. Mohammed Daud Bakar - Member
- H.H. Sh. Dr. Adham Al Said – Member
- Sh. Dr. Khalid Al Amri – Member
- Sh. Saleh Al Kharusi - Member

3.23 New standards, amendments and interpretations

3.23.1 New standards, amendments and interpretations effective from 1 January 2017

For the year ended 31 December 2017, the Window has adopted all of the amendments in standards issued by AAOIFI that are relevant to tis operations and effective for the period beginning on 1 January 2017.

3.23.2 Standard issued but not yet effective
FAS 30 Impairment, Credit losses and onerous commitments

In November 2017, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) issued Financial Accounting Standard (FAS) 30 - Impairment, credit losses and onerous commitments, the standard supersedes the earlier FAS 11 "Provisions and Reserves" effective from the financial periods beginning on or after 1 January 2020, with early adoption permitted.

However, during the year, the CBO has issued a circular BM 1149 dated 13 April 2017 governing implementation of IFRS 9 Financial Instruments (IFRS 9) for all the banks, which also apply to Islamic banks/windows subject to any specific instructions by the Central Bank for Islamic Banking entities on IFRS 9 if, as and when instructions are issued.

The Window has assessed the estimated impact of the initial application of IFRS 9 and its initial estimate is expected to impact total owner's equity by 1% – 2% as of 1 January 2018. This is preliminary, because not all transition work has been finalised. The actual impact of adopting IFRS 9 on 1 January 2018 may change accordingly.

4. CRITICAL ACCOUNTING JUDGMENT AND KEY SOURCES OF ESTIMATION UNCERTAINTY

4.1 Impairment

Impairment losses on financing

Management reviews its financing portfolio to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the statement of income, management makes judgment's as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of finances before the decrease can be identified with an individual receivable in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of customers in a group that correlates with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

4.2 Useful life of property and equipment

Depreciation is charged so as to write off the cost of assets over their estimated useful lives. The calculation of useful lives is based on management's assessment of various factors such as the operating cycles, the maintenance programs, and normal wear and tear using its best estimates.

5. CASH AND BALANCES WITH CENTRAL BANK OF OMAN ("CBO")

	2017 RO'000	2016 RO'000
Cash in hand	1,085	953
Balances with Central Bank of Oman ("CBO")	4,184	14,110
Cash and balances with Central bank of Oman ("CBO")	5,269	15,063

6. DUE FROM BANKS AND FINANCIAL INSTITUTIONS

	Self-Financed RO'000	Jointly Financed RO'000	Total 2017 RO'000
Due from Foreign Banks	1,905	2,858	4,763
Due from Local Banks	6,068	9,101	15,169
Due from banks and financial institutions	7,973	11,959	19,932
	Self-Financed RO'000	**Jointly Financed RO'000**	**Total 2016 RO'000**
Due from Foreign Banks	4,687	7,030	11,717
Due from Local Banks	35	52	87
Due from banks and financial institutions	4,722	7,082	11,804

7. FINANCIAL ASSETS

Financial assets held to maturity

	Self-Financed RO'000	Total 2017 RO'000
Government Sukuk	**963**	**963**
Manufacturing Sector Sukuk	963	963
Financial asset held for maturity	1,926	1,926

	Self-Financed RO'000	Total 2016 RO'000
Manufacturing Sector Sukuk	963	963
Financial asset held for maturity	963	963

Financial assets held for trade

	Self-Financed RO'000	Total 2017 RO'000
Government Sukuk	**3,000**	**3,000**
Banking Sector Sukuk	**550**	**550**
Financial asset held for trading	**3,550**	**3,550**

	Self-Financed RO'000	Total 2016 RO'000
Government Sukuk	3,000	3,000
Financial asset held for trading	3,000	3,000

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8. DEFERRED SALES UNDER MURABAHA

	Self-Financed	Jointly Financed	Total 2017
	RO'000	RO'000	RO'000
Gross deferred sales under Murabaha	**729**	**1,094**	**1,823**
Less: deferred profit under Murabaha	**(51)**	**(76)**	**(127)**
	678	**1,018**	**1,696**
Less: Provision for doubtful Murabaha	**(12)**	**(19)**	**(31)**
Deferred sales under Murabaha	**666**	**999**	**1,665**
	Self-Financed	**Jointly Financed**	**Total 2016**
	RO'000	**RO'000**	**RO'000**
Gross deferred sales under Murabaha	768	1,153	1,921
Less: Deferred profit under Murabaha	(59)	(89)	(148)
	709	1,064	1,773
Less: Provision for doubtful Murabaha	(17)	(26)	(43)
Deferred sales under Murabaha	692	1,038	1,730

The deferred sales under Murabaha pertain to finance provided to retail customers. The credit quality of the deferred sales under Murabaha that were neither past due nor impaired can be assessed by reference to the internal rating system adopted by Muzn.

Deferred sales receivables past due but not impaired

	2017 RO'000	2016 RO'000
Past due up to 30 days	**171**	62
Past due 30 – 60 days	**15**	7
Past due 60 – 89 days	-	11
Total	**186**	80

At 31 December 2017, impaired deferred sales under Murabaha receivables on which profit is being accrued or where profit has been reserved amounted to Nil (2016 – RO 9K).

9. IJARAH MUNTAHIA BITTAMLEEK – NET

	Self-Financed RO'000	Jointly Financed RO'000	Total 2017 RO'000
Cost			
At 1 January 2017	**41,360**	**62,040**	**103,400**
Additions - net	**3,962**	**5,942**	**9,904**
At 31 December 2017	**45,322**	**67,982**	**113,304**
Depreciation			
At 1 January 2017	**(7,298)**	**(10,947)**	**(18,245)**
Charge for the year	**(3,385)**	**(5,078)**	**(8,463)**
At 31 December 2017	**(10,683)**	**(16,025)**	**(26,708)**
Net book value at 31 December 2017	**34,639**	**51,957**	**86,596**
Less: provision for doubtful debts	**(458)**	**(686)**	**(1,144)**
Ijarah Muntahiah Bittamleek – net	**34,181**	**51,271**	**85,452**

	Self-Financed RO'000	Jointly Financed RO'000	Total RO'000
Cost			
At 1 January 2016	34,942	52,413	87,355
Additions – net	6,418	9,627	16,045
At 31 December 2016	41,360	62,040	103,400
Depreciation			
At 1 January 2016	(4,401)	(6,603)	(11,004)
Charge for the year	(2,896)	(4,345)	(7,241)
At 31 December 2016	(7,297)	(10,948)	(18,245)
Net book value at 31 December 2016	34,062	51,093	85,155
Less: provision for doubtful debts	(438)	(656)	(1,094)
Ijarah Muntahiah Bittamleek – net	33,624	50,437	84,061

The Ijarah Muntahia Bittamleek pertains to finance provided to retail and corporate customers. The credit quality of the Ijarah Muntahia Bittamleek that were neither past due nor impaired can be assessed by reference to the internal rating system adopted by Muzn.

Ijarah Muntahia Bittamleek past due but not impaired

	2017 RO'000	2016 RO'000
Past due up to 30 days	**12,121**	6,072
Past due 30 – 60 days	**1,861**	751
Past due 60 – 89 days	**154**	1,706
Total	**14,136**	8,529

At 31 December 2017, impaired Ijarah Muntahia Bittamleek on which profit is being accrued or where profit has been reserved amounted to RO 532K (2016 – RO 493K).

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10. DIMINISHING MUSHARAKA

	Self-Financed RO'000	Jointly Financed RO'000	Total 2017 RO'000
Diminishing Musharaka receivables	**4,448**	**6,672**	**11,120**
Less: Provision for doubtful receivables	**(44)**	**(68)**	**(112)**
Total	**4,404**	**6,604**	**11,008**

	Self-Financed RO'000	Jointly Financed RO'000	Total 2016 RO'000
Diminishing Musharaka receivables	4,882	7,322	12,204
Less: Provision for doubtful receivables	(49)	(73)	(122)
Total	4,833	7,249	12,082

Diminishing Musharaka pertains to finance provided to retail and corporate customers. The credit quality of the Diminishing Musharaka that were neither past due nor impaired can be assessed by reference to the internal rating system adopted by Muzn.

Diminishing Musharaka past due but not impaired

	2017 RO'000	2016 RO'000
Past due up to 30 days	**878**	1,981
Past due 30 – 60 days	**233**	779
Total	**1,111**	2,760

11. Forward Ijarah

	Self-Financed RO'000	Jointly Financed RO'000	Total 2017 RO'000
Forward Ijarah receivables	1,881	**2,822**	4,703
Less: Provision for doubtful receivables	(19)	**(28)**	(47)
Total	1,862	**2,794**	4,656

	Self-Financed RO'000	Jointly Financed RO'000	Total 2016 RO'000
Forward Ijarah receivables	2,920	**4,379**	7,299
Less: Provision for doubtful receivables	(29)	**(44)**	(73)
Total	2,891	**4,335**	7,226

Forward Ijarah pertains to finance provided to retail and corporate customers. The credit quality of the Forward Ijarah that were neither past due nor impaired can be assessed by reference to the internal rating system adopted by Muzn.

	2017 RO'000	2016 RO'000
Past due up to 30 days	584	421
Past due 30 – 60 days	44	37
Total	628	458

12. Property and equipment – net

	Motor vehicles, furniture and equipment RO'000	Leasehold improvements RO'000	Total RO'000
Cost			
1 January 2017	**927**	**614**	**1,541**
Additions	**399**	**87**	**486**
31 December 2017	**1,326**	**701**	**2,027**
Depreciation			
1 January 2017	**578**	**575**	**1,153**
Charge for the period	**197**	**78**	**275**
31 December 2017	**775**	**653**	**1428**
Net book value at 31 December 2017	**551**	**48**	**599**
Cost			
1 January 2016	742	614	1,356
Additions	185	-	185
31 December 2016	927	614	1,541
Depreciation			
1 January 2016	444	462	906
Charge for the period	134	113	247
31 December 2016	578	575	1,153
Net book value at 31 December 2016	349	39	388

13. Other assets

	2017 RO'000	2016 RO'000
Profit receivable	123	120
Advanced rent	93	101
Miscellaneous assets	30	40
	246	261

14. OTHER LIABILITIES

	2017 RO'000	2016 RO'000
Sundry creditors	111	135
Short Term payable	8	-
Profits payable	2,045	863
Forward Ijarah advances	1,190	1,031
Deferred profit under Murabaha	127	148
	3,481	2,177

15. PROVISIONS FOR CREDIT LOSS FINANCES & RECOVERIES AND RELEASE FROM PROVIONS OF CREDIT LOSS FINANCES

15.1 Portfolio Provision

	2017 RO'000	2016 RO'000
At 1 January	1,094	1,014
Provided during the year	-	80
Released during the year	(23)	-
At 31 December	1,071	1,094

15.2 Specific provision

	2017 RO'000	2016 RO'000
At 1 January	200	162
Provided during the year	9	38
Recovered during the year	(19)	-
At 31 December	190	200

16. Unrestricted investment account holders

	2017 RO'000	2016t RO'000
Mudaraba Savings account	4,600	3,999
Profit equalization reserve	254	198
Investment risk reserve	93	68
	4,947	4,265
Wakala deposit	47,826	60,882
Flex Wakala	61,683	53,236
	109,509	114,118
Total unrestricted investment account holders	114,456	118,383

There is Nil restricted investment as at 31 December 2017 (2016: Nil).
Basis of distribution of the profit between owners' equity and unrestricted investment accountholders

16. UNRESTRICTED INVESTMENT ACCOUNT HOLDERS (Continued)

The investment profits are distributed between owners' equity and unrestricted investment accountholders for the year ended 31 December 2017 and period ended December 2016 as follows:

	2017 Percentage	2016 Percentage
Unrestricted investment accountholders share	**40%**	40%
Mudarib share	**60%**	60%

The investment risk reserve at 0.5 percent is deducted from customer's share after allocating the Mudarib share of profit as per the approved policy in order to cater against future losses of unrestricted investment accountholders. Investment risk reserve will revert to the investment accountholders as per terms and conditions of Mudaraba contract.

The profit equalization reserve at 1 percent is the amount Muzn appropriates in excess of the profit to be distributed to unrestricted accountholders before allocating the Mudarib share of income to maintain a certain level of return. Profit equalization reserve will revert to owner equity and unrestricted investment accountholders.

17. ASSIGNED CAPITAL

The assigned capital consists of RO 13,500,000 transferred from National Bank of Oman SAOG. (31 December 2016: RO 13,500,000)

18. DEFERRED SALES UNDER MURABAHA PROFIT

	Self-Financed RO'000	Jointly Financed RO'000	Total 2017 RO'000
Deferred sales under Murabaha profit	34	52	86
	Self-Financed RO'000	**Jointly Financed RO'000**	**Total 2016 RO'000**
Deferred sales under Murabaha profit	39	58	97

19. Ijarah Muntahiah Bittamleek income

	Self-Financed RO'000	Jointly Financed RO'000	Total 2017 RO'000
Income from Ijarah Muntahiah Bittamleek	5,035	7,553	12,588
Less : depreciation	(3,385)	(5,078)	(8,463)
	1,650	2,475	4,125
	Self-Financed RO'000	**Jointly Financed RO'000**	**Total 2016 RO'000**
Income from Ijarah Muntahiah Bittamleek	4,260	6,389	10,649
Less : depreciation	(2,897)	(4,344)	(7,241)
	1,363	2,045	3,408

20. DIMINISHING MUSHARAKA INCOME

	Self-Financed RO'000	Jointly Financed RO'000	Total 2017 RO'000
Income from Diminishing Musharaka	264	397	661
	Self-Financed RO'000	**Jointly Financed RO'000**	**Total 2016 RO'000**
Income from Diminishing Musharaka	220	331	551

21. RETURN ON UNRESTRICTED INVESTMENT ACCOUNTHOLDERS

	2017 RO'000	2016 RO'000
Mudaraba Savings account	**33**	51
	33	51
Wakala	**1,650**	1,213
Flex Wakala	**1,378**	272
	3,028	1,485
	3,061	1,536

22. GENERAL AND ADMINISTRATIVE EXPENSES

	2017 RO'000	2016 RO'000
Salaries and allowances	**1,420**	1,333
Rent, rates and taxes	**219**	225
Publicity	**46**	134
Management fee to Head Office	**60**	53
Repair and maintenance	**83**	77
Legal and professional fees	**5**	53
Stationery	**19**	28
Directors' fees	**53**	51
Travel expenses	**27**	15
Miscellaneous expenses	**203**	191
	2,135	2,160

23. RELATED PARTY TRANSACTIONS

In the ordinary course of business, Muzn conducts transactions with certain of its Directors, shareholders and companies over which they are able to exert significant influence. The aggregate amounts of balances with such related parties are as follows:

	2017 RO'000	2016 RO'000
Deposits and other accounts		
Directors, Sharia Supervisors and shareholders holding less than 10% interest in Muzn	**6,940**	7,574
Financings		
Directors, Sharia Supervisors and shareholders holding less than 10% interest in Muzn	**120**	6

The income statement includes the following amounts in relation to transactions with related parties:

	2017 RO'000	2016 RO'000
Remuneration paid to Directors & Sharia Supervisory Board		
Chairman		
– remuneration proposed	**8**	8
– sitting fees paid	**3**	3
– other expenses paid	**3**	3
Other Directors		
– remuneration proposed	**19**	16
– sitting fees paid	**12**	16
– other expenses paid	**8**	5
Management fee payable to conventional banking	**60**	53

24. CONTINGENT LIABILITIES AND COMMITMENTS

24.1 Credit related contingent items

	2017 RO'000	2016 RO'000
Letters of credit	-	68
Letters of guarantee	**699**	101
	699	169

24.2 Capital and investment commitments

	2017 RO'000	2016 RO'000
Contractual commitments for Forward Ijarah	**2,017**	1,896
Operating lease commitments	**68,400**	227,100
Future minimum lease payments:		
Not later than one year	**20,400**	81,600
Later than one year and not later than five years	**48,000**	145,500
	68,400	227,100

25. FINANCIAL RISK MANAGEMENT

The primary objective of risk management is to safeguard the Muzn's resources from the various risks which Muzn faces. The Risk Group comprises of Corporate Credit Risk, Retail Credit Risk, Market Risk and Operational Risk. All risk management functions report to Chief Risk Officer and are independent from Business Units. Muzn has exposure to credit risk, liquidity risk and market risk.

Credit risk

Credit risk is the risk that Muzn will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations to Muzn. Muzn manages and controls credit risk by setting internal limits on the amount of risk it is willing to accept for individual counterparties and groups (single obligors) and industry sectors in line with the guidelines of Central Bank of Oman.

Credit risk management

To manage the level of credit risk, Muzn deals with counter-parties of good credit. Corporate Credit Committee of the Board is the final credit approving authority of Muzn which is mainly responsible for approving all credit proposals beyond the authority level of the management. The Management Credit Committee ("MCC") is the management decision making body which is empowered to consider all credit related issues up to certain limits.

Credit risk mitigation policies

Muzn manages, limits and controls concentrations of credit risk - in particular, with respect to individual counterparties and groups, and industries and countries. Muzn structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored and reviewed periodically by the Management Credit Committee and Board Risk Committee.

To facilitate risk mitigation Moody's, S&P and Fitch ratings have also been set up and are also being used as guidelines to ensure portfolio diversification in terms of sovereign risk ratings and geographical exposure. These limits are approved by the Board. Retail financing is strictly in accordance with the CBO guidelines.

The analysis of financing portfolio is provided below. It is pertinent to mention that the financing portfolio consists of all standard accounts and there is no impairment in the portfolio.

25. FINANCIAL RISK MANAGEMENT (Continued)

(a) Geographical concentrations

All the financial asset and financial liabilities reported in the balance sheet and all the items reported in off balance are based in Sultanate of Oman.

(b) Customer concentrations

On Assets	Due from Banks and financial institutions	Financial assets	Deferred sales under Murabaha Total	Ijarah Muntahia Bittamleek
31 December 2017	RO'000	RO'000	RO'000	RO'000
Retail	-	-	1,335	60,945
Corporate	19,932	5,476	331	24,507
	19,932	5,476	1,666	85,452

On Assets	Diminishing Musharak	Forward Ijarah
31 December 2017	RO'000	RO'000
Retail	546	3,271
Corporate	10,462	1,384
	11,008	4,655

On Liabilities 31 December 2017	Current accounts	Unrestricted Investment Accountholders
	RO'000	RO'000
Retail	1,135	16,546
Corporate	4,141	97,910
	5,276	114,456

On Assets 31 December 2017	Due from Banks and financial institutions	Financial assets	Deferred sales under Murabaha Total	Ijarah Muntahia Bittamleek
	RO'000	RO'000	RO'000	RO'000
Retail	-	-	1,585	59,881
Corporate	11,804	3,963	145	24,180
	11,804	3,963	1,730	84,061

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25. FINANCIAL RISK MANAGEMENT (Continued)

On Assets	Diminishing Musharaka	Forward Ijarah
31 December 2016	RO'000	RO'000
Retail	-	5,932
Corporate	12,082	1,294
	12,082	7,226

On Liabilities	Current accounts	Unrestricted investment accountholders
31 December 2016	RO'000	RO'000
Retail	1,191	14,473
Corporate	3,679	103,910
	4,870	118,383

(c) Economic sector concentrations

	Assets				Liabilities	
	Deferred sales under Murabaha	Ijarah Muntahiah Bittamleek	Diminishing usharaka	Forward Ijarah	Current accounts	Wakala and Savings deposit
	RO'000	RO'000	RO'000		RO'000	RO'000
31 December 2017						
Personal	1,334	60,944	546	3,271	5,276	114,456
Construction	11	16,714	10,206	1,354	-	-
Manufacturing	-	1,847	100	-	-	-
Trade	232	-	-	-	-	-
Services	88	5,947	156	-	-	-
	1,665	85,452	11,008	4,655	5,276	114,456

31 December 2016	Assets			Liabilities	
	Deferred sales under Murabaha	Diminishing Musharaka	Forward Ijarah	Current accounts	Wakala and Savings deposit
Personal	1,585	-	5,932	4,870	118,383
Construction	-	12,082	1,294	-	-
Manufacturing	-	-	-	-	-
Trade	145	-	-	-	-
Services	-	-	-	-	-
	1,730	12,082	7,226	4,870	118,383

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The movement of restructured loans is set out as below:

	2017 RO'000	2016 RO'000
At 1 January	-	1,021
Additions during the year	-	(1,021)
Balance at 31 December	-	-

Liquidity risk

Liquidity risk is the potential inability to meet Muzn's liabilities as they become due. It arises when Muzn is unable to generate cash to cope with a decline in deposits or increase in assets.

Muzn's liquidity risk management is governed by the Treasury Risk Policy document approved by the Board of Directors as well as the provisions of the relevant CBO guidelines on liquidity risk management through cash flow approach. The liquidity management does not only measure the liquidity position of the Bank on an going basis but also examine how funding requirement are likely to evolve under various scenarios.

Muzn monitors its liquidity risk through cash flow approach and stock approach. Under the cash flow approach, Muzn generates Maturity of Assets and Liabilities (MAL) report which captures all the maturing assets and liabilities into various pre-set time buckets ranging from one month to over five years. The mismatches in various time buckets indicate liquidity gap and Muzn strictly adheres to the CBO set limit of 15% of cumulative liabilities (outflows) on mismatches (liquidity gaps) in time buckets up to one year. In addition, Muzn has also set up internal limit on mismatches in time buckets beyond one year.

Treasury department of Muzn controls and monitors the liquidity risk and ensures that Muzn is not exposed to undue liquidity risk and at the same time makes optimum use of its funds. The middle office in Credit risk division also monitors the liquidity position of Muzn and provides the liquidity gap to Treasury Department to meet liquidity gaps.

The Central Bank of Oman has issued guidelines on the implementation of Basel III liquidity framework which are Liquidity Coverage Ratio (LCR) and Net Stable Funding (NSFR).

The Liquidity coverage ratio (LCR) is a short time ratio designed to increase resilience against a liquidity shortage of up to 30 days. The LCR is computed as per CBO requirement under the circular BM1127 (BASEL III: Framework on Liquidity coverage ratio and LCR disclosure standards). It is applicable from January 1, 2015 with a minimum ratio of 60% and increasing by 10% every year thereafter till it reaches a minimum required level of 100% on January 1, 2019.

The Net Stable Funding Ratio (NSFR) is a longer term structural ratio designed to address liquidity mismatches and reduce funding risk over a one year horizon. It is effective January 2018, with a minimum ratio of 100% as per the regulatory guidance.

25. FINANCIAL RISK MANAGEMENT (Continued)

Liquidity risk (Continued)

The residual maturity profile of the assets, liabilities and equity at 31 December 2017 is as follows:

31 December 2017	Due on demand and up to 30 days RO'000	More than 1 month to 6 months RO'000	More than 6 months to 12 months RO'000	More than 1 year to 5 years RO'000	Over 5 years RO'000	Total RO'000
Cash and balances with Central Bank of Oman	2,207	1,395	454	547	666	5,269
Due from banks and financial institutions	19,932	-	-	-	-	19,932
Financial assets:						-
- Held to Maturity	-	-	-	1,926	-	1,926
- Held for Trade	3,550	-	-	-	-	3,550
Deferred sales under Murabaha	52	292	230	1,034	57	1,665
Ijarah Muntahiah Bittamleek – net	1,142	4,361	4,464	34,055	41,430	85,452
Diminishing Musharaka	82	1,063	870	7,152	1,841	11,008
Forward Ijarah	231	246	572	3,607	-	4,656
Property and equipment (net)	-	-	-	-	599	599
Other assets	247	-	-	-	-	247
Total assets	27,443	7,357	6,590	48,321	44,593	134,304
Current accounts	5,276	-	-	-	-	5,276
Other liabilities	3,481	-	-	-	-	3,481
Unrestricted investment account holders	18,625	46,233	14,739	13,872	20,987	114,456
Owner's equity	-	-	-	-	11,091	11,091
Total liabilities and Unrestricted investment accountholders and owners' equity	27,382	46,233	14,739	13,872	32,078	134,304

The maturity profile of the assets, liabilities and equity at 31 December 2016 is as follows:

31 December 2016	Due on demand and up to 30 days RO'000	More than 1month to 6 months RO'000	More than 6 months to 12 months RO'000	More than 1 year to 5 years RO'000	Over 5 years RO'000	Total RO'000
Cash and balances with Central Bank of Oman	11,916	1,504	841	309	493	15,063
Due from banks and financial institutions	11,804	-	-	-	-	11,804
Financial assets						
Held For Maturity	-	-	-	963		963
Held for Trade	3,000	-	-	-		3,000
Deferred sales under Murabaha	48	321	243	1,009	109	1,730
Ijarah Muntahiah Bittamleek – net	1,270	2,718	4,332	32,138	43,603	84,061

25. Financial risk management (Continued)

Liquidity risk (Continued)

Diminishing Musharaka	172	652	1,114	7,600	2,544	12,082
Forward Ijarah	109	208	2,765	4,144	-	7,226
Property and equipment (net)	-	-	-	-	388	388
Other assets	261	-	-	-	-	261
Total assets	**28,580**	**5,403**	**9,295**	**46,163**	**47,137**	**136,578**
Current accounts	4,870	-	-	-	-	4,870
Other liabilities	2,177	-	-	-	-	2,177
Unrestricted investment account holders	17,542	48,240	26,922	10,228	15,451	118,383
Owner's equity	-	-	-	-	11,148	11,148
Total liabilities and unrestricted investment accountholders and owners' equity	24,589	48,240	26,922	10,228	26,599	136,578

	Total Unweighted Value (average)	Total Weighted Value (average)
	RO'000	RO'000
HIGH QUALITY LIQUID ASSETS	-	27,535
Total High Quality Liquid Assets (HQLA)	-	27,535
Cash outflows Retail deposits and deposits from small business customers of which:	**15,771**	**1,355**
Stable deposits	4,450	223
Less stable deposits	11,321	1,132
Unsecured wholesale funding, of which: Operational deposits (all counterparties) and deposits in networks of cooperative banks	68,149	24,034
Additional requirements, of which Credit and liquidity facilities	-	-
Other contingent funding obligations	565	50
TOTAL CASH OUTFLOWS	-	**25,438**
Cash Inflows		
Inflows from fully performing exposures	9,196	8,832
Other cash inflows	919	919
TOTAL CASH INFLOWS	10,115	9,751
TOTAL HIGH QUALITY LIQUID ASSETS	-	**27,535**
TOTAL NET CASH OUTFLOWS	-	**15,688**
LIQUIDITY COVERAGE RATIO (%)	-	**175.52**

Market risk

Market risk includes currency risk, profit rate risk and equity price risk.

(a) Currency risk

Muzn is exposed to currency risk through its transactions in foreign currencies. The major foreign currency to which Muzn is exposed is the US Dollar which is effectively pegged to Rial Omani. Muzn finances a significant portion of its financial assets in the same currencies as the relevant measurement currencies to mitigate its foreign currency risk.

25. FINANCIAL RISK MANAGEMENT (Continued

Liquidity Risk (Continued)

(b) Profit rate risk

Profit rate risk (PRR) is the risk that Muzn will incur a financial loss as a result of mismatch in the profit rates on assets & investment accountholders. The profit distribution to investment accountholders in based on Profit Sharing Agreements. Therefore, Muzn is not subject to any significant PRR. However, the profit sharing agreements will result in displaced commercial risk when Muzn's results do not allow it to distribute profits in line with the market rates.

Muzn has a detailed Profit Distribution Policy in place which details the process and management of Profit Distribution, including setting up of Profit Equalization & Investment Risk Reserve. The responsibility of profit rate risk management rests with Muzn's Asset and Liability Management Committee (ALCO).

Profit rate risk is managed by monitoring the sensitivity of the bank's financial assets and liabilities to various standardized profit rate shocks. Standardised shocks include a 100 basis point and 200 basis point parallel shifts in yield curves that are considered on a monthly basis. The impact of these shocks is analysed in the context of its impact on Earnings and Economic Value. The impact is compared against internal limits which have been formulated in line with the Central Bank of Oman and Basel Committee guidelines. The analysis is regularly reviewed by the Management and Board Risk Committee.

Earning impact of 200 basis points parallel shift in profit rate is provided below:

As at December 2017	200 bps increase	200 bps decrease
Earnings impact - RO'000s	128	(128)

Profit rate sensitivity gap

Sensitivity to profit rates arises from mismatches in the period to re-pricing of assets and that of the corresponding liability. Muzn manages these mismatches by following policy guidelines and reduces risk by matching the re-pricing of assets and liabilities.

31 December 2017	Effective average profit rate	Due on demand and within 6 months	Due within 7 to 12 months	Due within 1 to 5 years	Due after 5 years	Non-profit bearing	Total
	%	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Bank of Oman ("CBO")	N/A	-	-	-	-	5,269	5,269
Due from banks and financial Institutions	1.3%	19,931	-	-	-	1	19,932
Financial assets:							
- Held to Maturity	6.5%	-	-	1,926	-	-	1,926
- Held for Trade	4.3%	3,550	-	-	-	-	3,550
Deferred sales under Murabaha	4.7%	344	230	1,034	57	-	1,665
Ijarah Muntahia Bittamleek – net	5.3%	5,503	4,464	34,055	41,430	-	85,452
Diminishing Musharaka	5.3%	1,145	870	7,152	1,841	-	11,008
Forward Ijarah	N/A	-	-	-	-	4,656	4,656
Property and equipment – net	N/A	-	-	-	-	599	599
Other assets	N/A	-	-	-	-	247	247
Total assets		30,473	5,564	44,167	43,328	10,772	134,304

25. FINANCIAL RISK MANAGEMENT (Continued)

(b) Profit rate risk (continued)

31 December 2017	Effective average profit rate	Due on demand and within 6 months	Due within 7 to 12 months	Due within 1 to 5 years	Due after 5 years	Non- profit bearing	Total
	%	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Current accounts	N/A	-	-	-	-	5,276	5,276
Other liabilities	N/A	-	-	-	-	3,481	3,481
Unrestricted investment accountholders	2.4%	64,858	14,739	13,872	20,640	347	114,456
Owners' equity	N/A	-	-	-	-	11,091	11,091
Total liabilities and owners' equity		64,858	14,739	13,872	20,640	20,195	134,304
On-balance sheet gap		(34,385)	(9,175)	30,295	22,688	(9,423)	-
Cumulative profit sensitivity gap		(34,385)	(43,560)	(13,265)	9,423	-	-
31 December 2016							
Cash and balances with Central Bank of Oman "CBO")	N/A	-	-	-	-	15,063	15,063
Due from banks and financial Institutions	0.7%	11,778	-	-	-	26	11,804
Financial assets held for trading		-	-	-	-	-	-
- Held for Maturity	8.5%	-	-	963	-	-	963
-Held for Trade	3.5%	3,000	-	-	-	-	3,000
Deferred sales under Murabaha	4.8%	369	243	1,009	109	-	1,730
Ijarah Muntahia Bittamleek – net	5.1%	3,988	4,332	32,138	43,603	-	84,061
Diminishing Musharaka	5.4%	824	1,114	7,600	2,544	-	12,082
Forward Ijarah	N/A	-	-	-	-	7,226	7,226
Property and equipment – net	N/A	-	-	-	-	388	388
Other asset	N/A	-	-	-	-	261	261
Total assets		19,959	5,689	41,710	46,256	22,964	136,578
Current accounts	N/A	-	-	-	-	4,870	4,870
Other liabilities	N/A	-	-	-	-	2,177	2,177
Unrestricted investment accountholders	1.1%	65,782	26,922	10,228	15,185	266	118,383
Owners' equity	N/A	-	-	-	-	11,148	11,148
Total liabilities and owners' equity		65,782	26,922	10,228	15,185	18,461	136,578
On-balance sheet gap		(45,823)	(21,233)	31,482	31,071	4,503	-
Cumulative profit sensitivity gap		(45,823)	(67,056)	(35,574)	(4,503)	-	

Muzn Islamic Banking
Notes to Financial Statement 2017

(c) Equity risk

Currently, Muzn is not exposed to any Equity risk.

Operational risk

Muzn has adopted the Basic Indicator Approach under Basel II for the purpose of measuring capital charge for Operational Risk. The approach requires Muzn to provide 15% of the average three years gross annual income as capital charge for operational risk.

26. CAPITAL RISK MANAGEMENT

Muzn manages its capital to ensure that it will be able to continue as a going concern while maximising the return to shareholders within acceptable risk return framework. Muzn's overall strategy remains the same as applicable for Head Office.

The capital adequacy for Muzn is set out as below:

	2017	2016
	RO'000	RO'000
Assigned capital	13,500	13,500
Accumulated losses	(2,409)	(2,352)
Tier I capital	11,091	11,148
General loan loss impairment	913	906
Tier II capital	913	906
Total capital available	12,004	12,054
Risk weighted assets (RWA)		
Credit risk	73,071	72,505
Market risk	3	1
Operational risk	4,572	3,583
Total RWA	77,646	76,089
Capital ratios		
Total capital ratio	15.5%	15.8%
Total Tier I ratio	14.3%	14.7%

27. SEGMENTAL INFORMATION

Muzn is organised into three main business segments:

1) Retail banking – incorporating private customer current accounts, savings, deposits, deferred sales under Murabaha, Ijarah Muntahia Bittamleek, Forward Ijarah and Diminishing Musharaka.
2) Corporate banking – incorporating corporate customer current accounts, savings, deposits, deferred sales under Murabaha, Diminishing Musharaka, Ijarah Muntahia Bittamleek and Forward Ijarah.
3) Treasury and investments

Other operations comprise investment management and institutional finance neither of which constitutes a separately reportable segment.

Segment assets and liabilities comprise operating assets and liabilities, being the majority of the statement of financial position, but exclude items such as taxation and deposits.

Internal charges and transfer pricing adjustments have been reflected in the performance of each business. Revenue sharing agreements are used to allocate external customer revenues to a business segment on a reasonable basis.

27. SEGMENTAL INFORMATION (Continued)

At 31 December 2017	Retail banking	Corporate banking	Treasury and investments	Other	Total
	RO'000	RO'000	RO'000	RO'000	RO'000
Segment operating revenues	2,841	2,030	141	-	5,012
Other revenues	70	76	268	35	449
Segment operating revenues	2,911	2,106	409	35	5,461
Profit expenses	(300)	(2,761)	-	(81)	(3,142)
Net operating income	2,612	(655)	409	(46)	2,319
Segment cost Operating expenses including depreciation	(963)	(246)	(84)	(1,117)	(2,410)
Impairment for finances net of allowance for provision	23	10	-	-	33
Net Profit for the year	1,671	(891)	325	(1,163)	(57)
Gross segment assets	67,878	37,321	29,592	846	135,637
Less: Impairment allowance	(697)	(636)	-	-	(1,333)
Segment assets	67,181	36,685	29,592	846	134,304
Segment liabilities	17,334	102,051	11,091	3,828	134,304

At 31 December 2016	Retail banking	Corporate banking	Treasury and investments	Other	Total
	RO'000	RO'000	RO'000	RO'000	RO'000
Segment operating revenues	2,472	1,584	14	-	4,070
Other revenues	70	26	164	23	283
Segment operating revenues	2,542	1,610	178	23	4,353
Profit expenses	(1,420)	(93)	(23)	(36)	(1,572)
Net operating income	1,122	1,517	155	(13)	2,782
Segment cost					
Operating expenses including depreciation	(952)	(209)	(51)	(1,196)	(2,408)
Impairment for finances net of allowance for provision	(53)	(65)	-	-	(118)
Net profit for the year	117	1,243	104	(1,209)	255
Gross segment assets	69,033	38,352	29,877	649	137,911
Less: Impairment allowance	(715)	(618)	-	-	(1,333)
Segment assets	68,318	37,734	29,877	649	136,578
Segment liabilities	15,398	107,589	11,148	2,443	136,578

28. CORRESPONDING FIGURES

Corresponding figures have been rearranged and reclassified, wherever necessary for the purpose of comparison and for better presentation, the effect of which is not material.

NBO's Branch Network

• **59** Branches in Oman • **15** Sadara Centres • **6** Muzn Islamic Banking Branches • **2** Branches in UAE

Branch	Telephone No	
Azaiba - HO Branch	24778190	24778355

MUSCAT SOUTH REGION BRANCHES

Branch	Telephone No	
Hamriya	24831520	24833792
Corniche	24715103	24714245
Wattaya	24568244	24560585
Qurriat	24846100	24846415
MAF	24565561	24566860
Qurum	24560050	24562615
CBD	24778350	24778351
Amerat	24875766	24877379
Shati Qurum	24607161	24607687

MUSCAT NORTH REGION BRANCHES

Branch	Telephone No	
Al Mawaleh	24511164	24511165
Bousher	24587291	24587294
Ministry Of Health	24692310	24692309
Al Khoudh	24537950	24537951
Seeb Town	24420441	24423511
Maabella	24453314	24455957
Ghoubra	24497229	24491062
Bukha	26828014	
Airport	24521448	24510007
Khasab	26731442	26730467
Al Khuwair	24486441	24486481
Sultan qaboos university	24446768	24446556

Dakhliya & Dhahira REGION BRANCHES

Branch	Telephone No	
Nizwa	25413169	25410072
Buraimi	25653037	
Ibri	25691161	
Bahla	25363613	25363786
Sumail	25350355	
Fanja	25361190	
Al Hamra	25422008	
FIRQ	25432149	
Dhank	25676603	
Araqi	25694342	

BATINA REGION BRANCHES - CONTACT DETAILS

Branch	Telephone No	
AFI	26780972	26781562
RUSTAQ	26878334	26878332
SOHAR AL HAMBAR	26859105	26859104
SHINAS	26748394	26747663
BARKA	26882007	
KHABOURAH	26802380	26805155
MUSNA	26870182	26871118
SAHAM	26855299	26855146
BIDAYA	26709340	26709240
SOHAR IND.	26755878	26755875
AL SUWAIQ	26860518	
SOHAR	26840234	26843780
LIWA	26762073	26762075

SHARQIYA REGION BRANCHES

Branch	Telephone No	
Ibra	25570144	25570015
Sur	25545158	25540246
Al Kamil	25557524	25558254
Bani Bu Ali	25554015	25554138
Jalaan	25550020	25550110
Masirah	25504516	25504026
Al Mudhaibi	25578484	25578014
Sinaw	25524212	25524223
Duqum	25427101	25427130

DHOFAR REGION BRANCHES

Branch	Telephone No	
Salalah	23291346	23291601
SQH	23211092	23211042
Mirbat	23268345	23268346
Saada	23225283	23226031
NEW SALALAH	23298027	23298037

DHOFAR REGION BRANCHES

Branch	Telephone No
Azaiba New HO	24778134
CBD	24778002
Mina Al Fahal	24565163
Al Khuwair	24487356
Shatti Al Qurum	24607012

DHOFAR REGION BRANCHES	
Branch	Telephone No
Al Mawaleh Centre	24348118
Al Khoud Centre	24271367
Barka Centre	26882007
Saham Centre	26855146
Sohar Industarial Area	26755889
Nizwa Firq Center	25431122
Sur Centre	25545414
Sohar Hambar Centre	26859103
Salalah Centre	23291346
Rustaq centre	26878334

Muzn Islamic banking		
Branch	Telephone No	
Azaiba	24617013	24617014
Sur	25540642	
Sohar	26846698	
Nizwa	25411241	25411681
Salalah	23289230	23291310
Maabella	24452387	24458304

UAE	
Branch	Telephone No
Abu Dhabi	97126974000
Dubai	97143049400